ISSN (Online): 2582-7928

Indian Public Policy Review

A Journal of Economics, Politics, and Strategy

VOLUME 3 MARCH 2022 ISSUE 2

ARTICLES

INDIAN PUBLIC POLICY REVIEW

IPPR is a peer-reviewed, bi-monthly, online, and an open-access journal. The objective of the journal is to further the cause of both research and advocacy by providing a publication space for articles in economics, politics, and strategic affairs. The journal publishes analytical papers – both theoretical and applied, with relevance to Indian public policy issues.

We welcome original papers, book reviews, and commentaries across the following topics: Economics, Political Science, Public Finance, International Relations and Security, Political and Defence Strategy, Public Enterprises, and Science and Technology Policy, among others.

Contact: editor@ippr.in

Journal Publishers

The Takshashila Institution,
2nd floor, 46/1, Cobalt Building, Church St, Haridevpur,
Shanthala Nagar, Ashok Nagar, Bengaluru - 560001

Indian Public Policy Review 2022, 3(2): 1-14

What Does Oil in Triple Digits Mean for India? Macroeconomic Implications and Policy Trade-offs

Sajjid Z. Chinoy

Toshi Jain*

Abstract

The Russia-Ukraine conflict is expected to impact India's economy through several channels but we posit first order impacts will emanate from higher crude prices. If crude prices were to average $100/barrel in 2022, they will constitute a discernible adverse terms of trade shock for India's economy that could shave a percentage point off India's growth, pressure inflation further and widen the current account deficit towards 3% of GDP. How should policy respond? A negative terms of trade shock would argue for a more depreciated equilibrium real effective exchange rate. Policymakers should let this adjustment gradually take place to enable the corresponding "expenditure switching" needed to bring external imbalances back to sustainable levels. A sustained supply shock will make the trade-off for monetary policy more acute, with downside risks to growth accompanied by upside risks to inflation expectations. While the 2022-23 Budget created buffers to protect against shocks, fiscal policy will face its own set of trade-offs in simultaneously attempting to accommodate the shock, support growth and preserve macroeconomic stability. Beyond the near term, policymakers must consider systematically hedging crude price imports in global markets to protect the economy from periods of outsized volatility, apart from the medium-term objective of reducing dependence on imported crude.

Keywords: Commodity Price Impact, Terms of Trade, GDP growth, Exchange Rate, Monetary Policy, Fiscal Policy, Current Account Deficit

JEL Codes: E61, E63, F32

Publication Date: 18 March 2022

---

* Sajjid Z. Chinoy and Toshi Jain are Chief India Economist and India Economist at J.P. Morgan, respectively

I Russia-Ukraine Conflict: Channels of Transmission

The Russia-Ukraine conflict is likely to impact India's economy through several different channels but it's important to separate the wheat from the chaff. The first-order impact, in our view, emanates from the negative terms of trade (ToT) shock on account of higher commodity prices, particularly crude prices, of which India imports about 85% of its requirements.

There are several other channels: a direct trade channel to the affected region, an indirect trade channel from weaker global -- particularly European -- growth, and a potential tightening of financial conditions and capital flows as global risk appetite ebbs and flows. However, these channels can be expected to be relatively second-order vis-a-vis the commodity price shock[1].

II 1.2% of GDP Terms of Trade shock from oil at $100

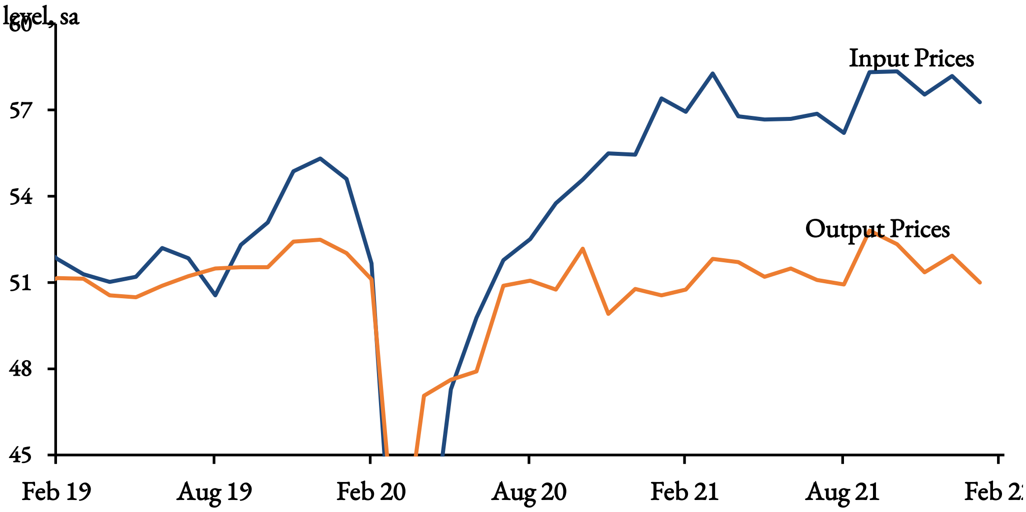
In turn, the bulk of the commodity price shock is expected to flow through crude prices. Upon commencement of the conflict, crude surged past $100/barrel -- and though there is likely to be an element of overshooting -- there is a growing expectation that, as the conflict gets more entrenched, crude prices could remain elevated for longer. The J.P. Morgan house view, for example, expects crude to average about $100/barrel for 2022 (calendar year) as of March 15. This would constitute a $30/barrel increase from the $70/barrel witnessed in 2021, and thereby constitute a discernible negative terms of trade shock for an oil-importing country such as India. Every $10/barrel in crude pieces increases India's net import bill by 0.4% of GDP. Therefore, crude at $100/barrel would accumulate into an adverse terms of trade (ToT) impact of 1.2% of GDP in 2022 vis-a-vis 2021. Put simply, the economy would be transferring out an incremental 1.2% of GDP for the same net oil imports (crude imports adjusted for petroleum product exports).[2] Back in 2014-15, the fall in crude prices at the time had delivered a 2% of GDP windfall across four quarters, as we had documented and analysed at the time (Chinoy and Jain, 2015). Now, the shoe is on the other foot.

To be sure, there will be impacts from other commodity prices, too. Higher coal and gas prices will add to the negative ToT pressures. In contrast, rising aluminium and steel prices (commodities that India exports) and wheat prices (an agricultural export that India could ramp up significantly) could mitigate some of those pressures. The net impact of these opposing dynamics is therefore likely to be more modest. Instead, the primary impact is likely to flow through oil prices.

III An Adverse Supply Shock

An adverse terms of trade shock is akin to a negative supply shock that simultaneously hurts growth, pushes up inflation and pressures external imbalances. The growth impact will manifest through constraints on fiscal space, an impingement of household purchasing power, and compressed firm margins. For example, if policymakers cut excise duties on petroleum products to ensure retail prices don't increase further (something we discuss more fully below), growth pressures will emanate from less expenditure space for any given fiscal deficit. In contrast, to the extent that retail prices move up further, household purchasing power will be squeezed with implications for private consumption growth. Similarly, if firm input costs rise but firms are unable to pass these on in the form of output price increases, firm margins and earnings – already under some pressure (see Figure 1) -- will come under further pressure.

Figure 1: India's Composite PMI: Input and Output Prices



Source: Markit

Therefore, the growth impact will manifest across several channels. Importantly, the quantum of the growth hit will be a function of the burden sharing between the government, households, and firms, because of the different marginal propensities to consume across these entities, as we discuss in more detail below.

IV Fiscal has already absorbed one-third of the shock thus far

When oil prices collapsed at the start of pandemic, India's policymakers successively raised excise duties on petroleum products, such that the fiscal garnered much of the oil windfall at the time. Duties on petrol and diesel were raised by Rs13-16/litre, garnering about 1% of GDP in oil tax revenues.

Now, as crude prices have moved up, these duties have been partially rolled back. The government cut duties by Rs10/litre for diesel and Rs5/litre for petrol in November, 2021. The fiscal cost of those cuts will amount to incremental lost revenue of 0.4% of GDP in 2022 over that borne in 2021. Effectively, therefore, the government has already absorbed 0.4% of GDP -- one-third of the 1.2% of GDP hit if oil averages $100.

This, of course, is not costless. The growth impact is the foregone fiscal expenditure on account of lower revenues. Excise duties were budgeted 0.4% of GDP lower in the 2022-23 Budget, correspondingly reducing space for more spending next fiscal year.

V Burden-Sharing: Three Scenarios and the Growth Impact

Put differently, the fiscal has already absorbed the increase from $70/barrel to $80/barrel. The question is how the next $20/barrel will be shared among the fiscal, households and firms, and what the corresponding growth implications will be?

Table 1 lays out three scenarios of burden-sharing across the different economic entities, to demonstrate how the growth impact is contingent on how the shock is distributed. In Scenario 1, retail prices are kept constant at current levels, such that the entire under-recovery is offset by further excise duty cuts. In essence, the fiscal takes on the entire hit[3]. The second scenario envisions half the residual hit taken by the fiscal and half passed on to the private sector. The third scenario envisions the entire residual hit passed on to the private sector.

In case of the fiscal absorbing the shock, with the central deficit already pegged at 6.4% of GDP for 2022-23, the growth impact is the foregone expenditure on account of lower revenues from a further cut in excise duties[4]. We agnostically assume a fiscal multiplier of 1, such that the corresponding expenditure hit translates into a commensurate hit to growth. To be sure, authorities could protect expenditures and let the deficit widen by a commensurate amount – which would be tantamount to pushing out the impact to the future and incurring higher public debt -- but that will have other risks and costs, as we discuss later.

In case of households, the growth hit occurs through a purchasing power hit from higher prices, net of any tax cuts[5]. In the first scenario, tax cuts may ensure no change to gasoline and diesel prices, but there are other components of the CPI basket that will still rise from higher crude prices that authorities cannot directly influence. In general, we use the RBI's estimates – that every 10% increase in crude prices pushes up headline CPI by 30 bps -- to quantify the cumulative impact. Finally, we assume a marginal propensity to consume out of income of 0.7 for households. To clarify, this is simply the impact of higher crude prices. To the extent that commodity prices pick up more broadly, the impact on inflation and the household purchasing power will be higher.

By construction, the residual ToT shock – after computing that borne by the public sector and households – is borne by corporates through margin pressures and a hit to profits. Like for households, the marginal propensity to invest from retained earnings is presumed to be less than 1.[6]

VI A 90-110 bps hit on growth

All told, the cumulative hit to growth is estimated to be 90-110 bps under different scenarios of burden-sharing. The greater the fraction borne by the fiscal, the larger the cumulative hit, because the marginal propensity to spend of the budget will be 1 – if this year's deficit target is unchanged – vis-a-vis a smaller marginal propensity to consume/invest for households and firms.

Table 1: Terms of Trade Shock Distribution (% of GDP)

	Scenario 1	Scenario 2	Scenario 3
Fiscal impact	1.0	0.7	0.4
Household	0.0	0.2	0.4
Corporate	0.2	0.3	0.4
ToT Shock	*1.2*	*1.2*	*1.2*
GDP impact	*1.1*	*1.0*	*0.9*

Source: J.P. Morgan

VII Contextualising the growth hit

To put this in perspective, it's important to understand the state of activity before the oil price shock. Recall, GDP contracted 6.6% in the pandemic year and the government's advance estimates peg growth at 8.9% in 2021-22, though downside risks have emerged in light of the Russia-Ukraine geo-political conflict. However, looking at annual growth rates do not necessarily reveal how complete the recovery has been from the COVID-19 shock. Instead, to assess that, we must contrast activity vis-à-vis a counter-factual pre-pandemic path to compare levels.

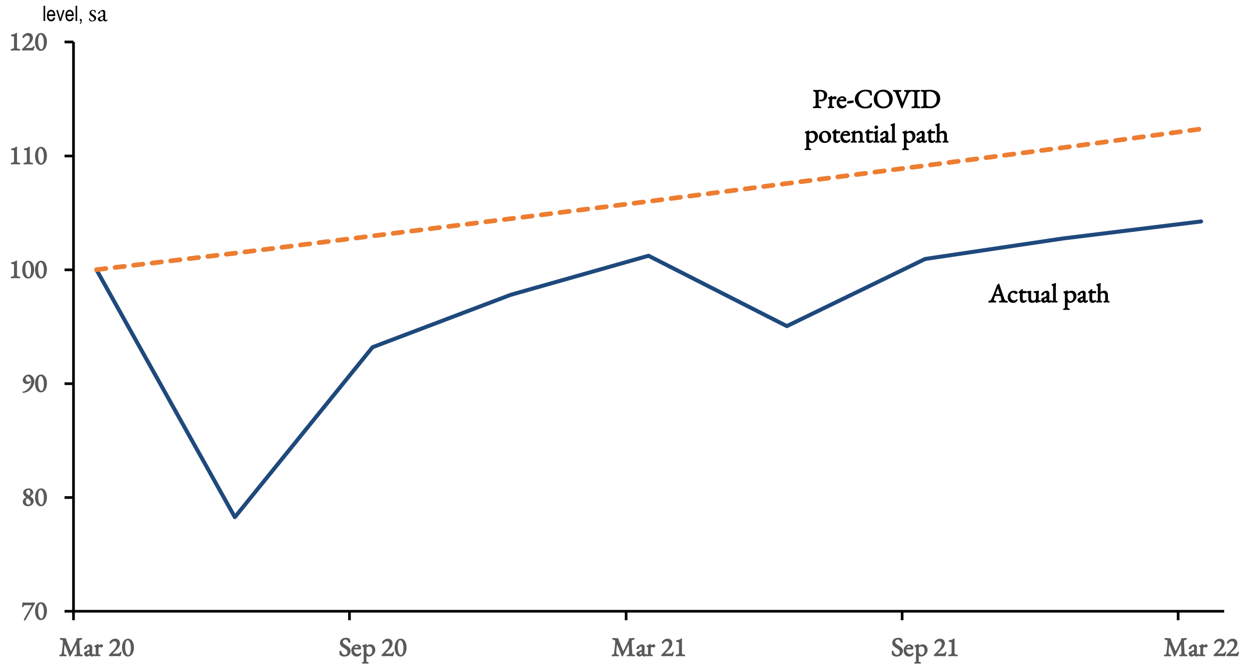
Figure 3 below maps out a counter-factual GDP path based on 6% growth, absent the pandemic. It then compares the actual GDP path from the pandemic to it. What do we find? That by March 2022, the level of GDP would still be about 7% below its pre-pandemic path. To be sure, all emerging markets will be below their pre-pandemic potential path to different degrees. But a 7% shortfall is meaningful. An oil shock that shaves off a percentage point of GDP growth in 2022 against this backdrop will therefore be non-trivial.

Aggregate shortfalls apart, what was expected to drive growth absent the oil-shock, and how does the latter change the growth-driver calculus? We have long postulated (see, Chinoy and Jain, 2021a) that private consumption and private investment will take time to recover. Even as private consumption has finally surpassed its pre-pandemic levels, it remains much below its pre-pandemic path and has been the slowest to recover across the different constituents of demand. This is unsurprising given evidence of scarring in the labour market and the hit to household balance sheets. Therefore, a more complete jobs recovery will need to serve as a pre-requisite to a sustainable consumption recovery. Rising inflation from a commodity price shock that impinges on household purchasing power will simply serve as an additional headwind to consumption.

In case of private investment, balance sheets have witnessed a significant improvement with large corporates deleveraging in recent years, such that the twin-balance sheet problem appears to be much less of a binding constraint on investment prospects. Instead, the current constraint appears to be demand, with manufacturing utilisation rates still in their mid-60s. Commodity producing sectors will clearly benefit from current developments. But commodity users face the prospect of margin and earnings pressures, quite apart from an increase in macroeconomic uncertainty.

With private consumption and investment expected to take time to recover, the heavy lifting for near term growth was expected to be undertaken by government spending – especially on infrastructure – and exports growth. However, to the extent that global growth will come under pressure from the Russia-Ukraine geo-political conflict, the outlook for exports has become more uncertain. This simply increases the onus for government spending, and fiscal policy, to support near term growth. But precisely when the onus on government spending has increased, so have the constraints with fiscal space expected to be eaten by higher crude and commodity prices. All this increases the policy challenge and creates several delicate fiscal trade-offs, as we discuss more fully later in this piece.

Figure 2: GDP Levels: Actual Versus Counter-Factual



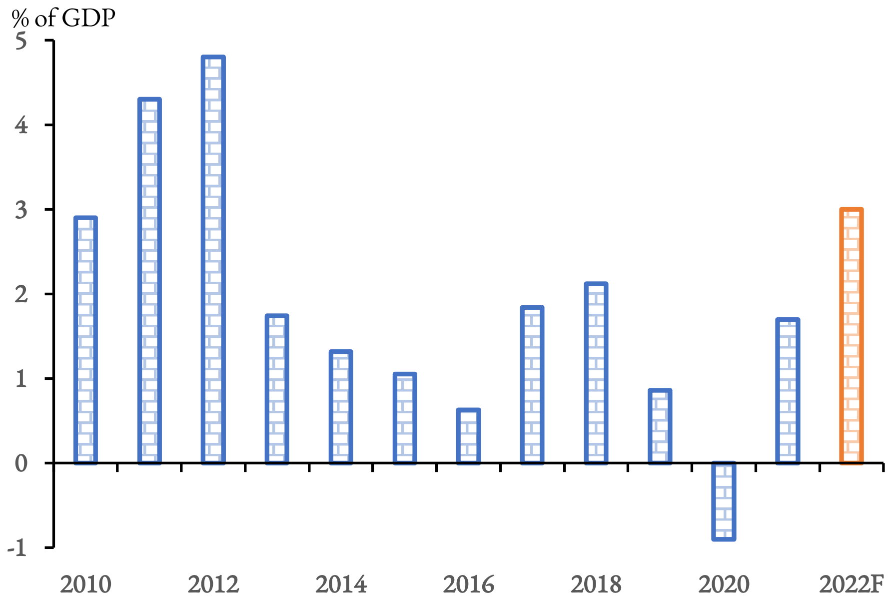
Source: J.P. Morgan

VIII Current Account: A New Normal?

Growth pressures apart, oil prices close to triple digits will also leave a sizeable imprint on the external sector, an area that policymakers have not had to worry about in recent years. India's current account deficit (CAD) has averaged just 1.1% of GDP in the seven years before the pandemic, reflecting, in part, lower crude and commodity prices. This has typically resulted in large BoP surpluses, a "problem of plenty" for the RBI and upward pressures on the rupee. These dynamics were accentuated in the pandemic when the current account went into surplus and the BoP surplus and FX reserves ballooned.

But things are fast changing. The quarterly CAD in the October-December quarter is expected to print close to 3% of GDP in a quarter when crude averaged $80/barrel. To be sure, it was also a quarter when non-oil, non-gold imports surged as the economy continued to open. There was an expectation that the CAD would mean-revert in 2022 as supply chains and goods prices normalised and global growth re-accelerated. Instead, if crude were to average $100/barrel (with every $10 increase adding 0.4% of GDP to the CAD), coal prices remain elevated and the value of gold imports – which have increased sharply over the last two years – remain elevated, the CAD in 2022-23 would be expected to average 3% of GDP, with risks skewed to the upside (Figure 3).

Figure 3: Current Account Deficit

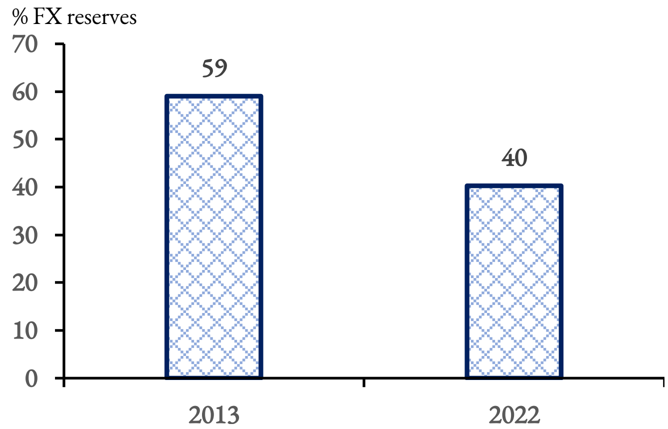


Note: 2022 refers to fiscal year FY23 and is the forecasted CAD based on crude at $100/barrel

Source: RBI, J.P. Morgan

This, in conjunction with tighter global financial conditions that may slow capital inflows into emerging markets, could presage some pressures on the BoP, for the first time in years. To be sure, there is no imminent macro-stability threat, given the war chest of FX reserves that the RBI possesses. For example, FX Reserves as a multiple of monthly imports is almost twice as large as was the case before the Taper Tantrum of 2013 while short-term debt as a fraction of FX reserves is much lower than in 2013 (see Figure 4).

Figure 4: Short Term Debt (Residual Maturity Basis)



Source: RBI

That said, after a long time, the current account and balance of payments will need close monitoring. Furthermore, these developments will have important implications for exchange rate policy, as we discuss below.

IX Inflation: From One Supply Shock To Another

Finally, rising commodity prices are expected to pressure inflation. Before the recent geopolitical tensions, we had expected headline CPI to average 5% in 2022-23, but this was predicated on oil at $80/barrel and some normalisation of supply chains in the coming months. The expectation was that services prices would rise as services demand finally normalised (with firms in the non-tradable sector making up for income losses of the last two years against the backdrop of relatively inelastic services demand), but this would be offset by goods prices disinflating as supply chains normalise and households switch expenditures from goods to services as the latter re-opens.

The Russia-Ukraine conflict could materially change this calculus. Not only are energy prices higher, but some supply chains are likely to be disrupted again, resulting in renewed cost push pressures in the goods sector and further margin compression, thereby creating fresh inflation risks. The RBI estimates that every 10% increase in crude prices increases headline CPI by 30 bps (both the direct and indirect impact). Mechanically, the move from $80 to $100 should therefore add about 75 bps. However, much will depend on whether taxes are cut and the fiscal absorbs some of this hit, as well as on the ability of firms to pass this on, since growth will also be hit by the oil shock. All told, we expect headline CPI to average between 5.5-6% in FY23, especially because the crude price increase will likely be accompanied by a pickup in other commodity prices, too.

X Policy Implications and Trade-Offs

All told, we find that crude at $100/barrel in 2022 could shave off 90-110 bps of GDP growth in India, widen the current account deficit to 3% of GDP, and potentially push up CPI by another 50-75 bps. How should policymakers respond and what are the associated trade-offs? We discuss these issues in subsequent sections.

1. External Sector and the Rupee

Perhaps the clearest prescription is on the external front. The widening of the CAD and associated BoP pressures will create some depreciation pressures on the rupee. We believe policymakers should let the Rupee reach this new equilibrium – albeit in a gradual and non-disruptive manner – and not prevent this adjustment. This is because, more fundamentally, a persistent negative terms of trade (ToT) shock will argue for a weaker equilibrium real effective exchange. Enabling this adjustment is therefore important in facilitating the necessary “expenditure switching” to reduce imports, boost exports and help narrow an elevated CAD (Figure 5). All told, a real depreciation of the currency that acts as a shock absorber for the economy is the optimal response to a negative ToT shock.

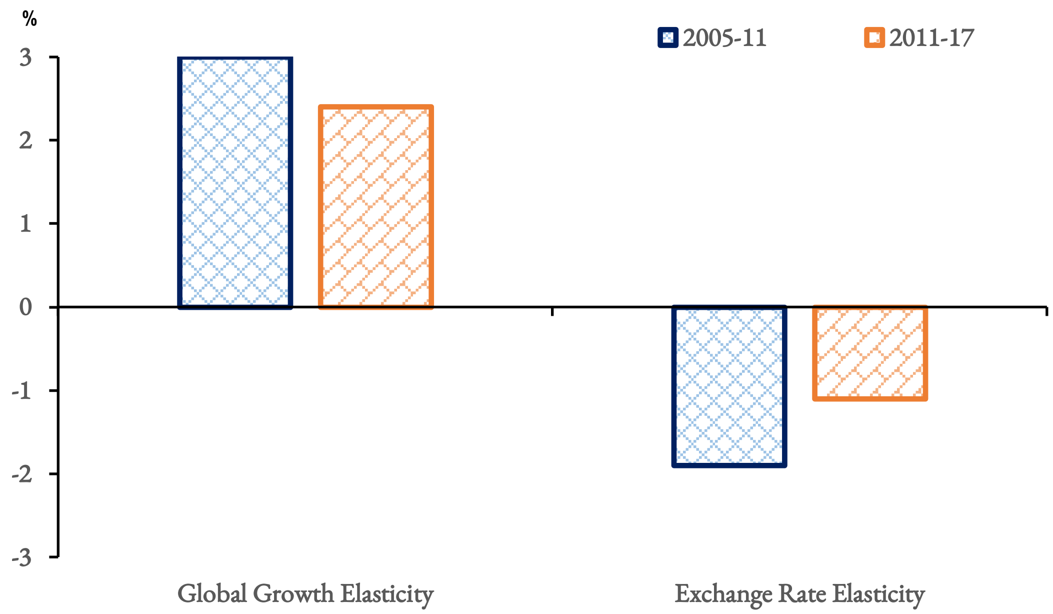
Figure 5: 40-Currency Real Effective Exchange Rate (REER)

Index 2015-16=100

Source: RBI

All this, however, presumes that exchange rate elasticities of India's exports and imports are non-negligible and that exchange rate depreciations are not contractionary, wherein balance sheet pressures from depreciation swamp the more beneficial impacts of modest trade elasticities. These concerns should be allayed in the case of India. We have previously found (Chinoy and Jain (2018)) that export elasticities to exchange rate movements, although having attenuated in recent times, still remain very healthy (Figure 6) – a finding robust to different specifications and controls – and consistent with other work on this topic (IMF, 2015). Similarly, work by Hsing (2010) and the RBI (Annual Report, 2015) reveals that exchange rate elasticities also matter on the import side, such that the Marshall-Lerner condition is met. All told, evidence would suggest that a trade-weighted real effective exchange rate depreciation would have a beneficial impact on India's external imbalances, even if J-curve effects are initially observed.

Figure 6: India's Export Elasticities



Source: Chinoy and Jain (2018)

2. Monetary Policy

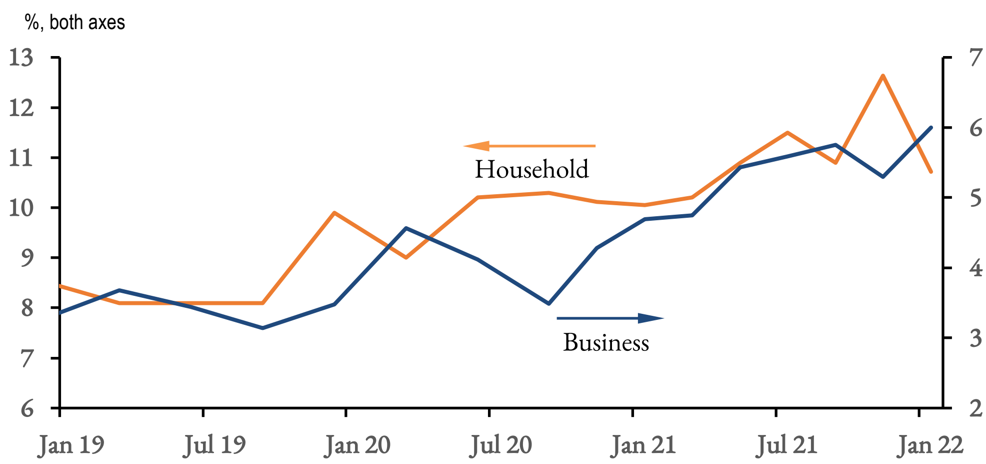
While a real deprecation can be expansionary, it can also be inflationary on account of a greater pass-through of import prices and, more fundamentally, by generating an aggregate demand boost in the wake of an adverse supply shock. With inflation sticky over the last two years, exchange rate depreciation would simply add to these pressures. How, then, should policy respond?

In a critical insight seven decades ago, Nobel laureate James Meade postulated that developing economies must strive to simultaneously achieve both "external balance" and "internal balance." But two objectives require two instruments. Johnson (1958) and Cordon (1960) labelled these "expenditure switching" and "expenditure control." In the current context, a real devaluation would help with expenditure-switching to narrow external imbalances. But is expenditure-control – in the form of tighter fiscal and monetary policy – warranted against the backdrop of sticky inflation accentuated by currency depreciation?

The dilemma for monetary policy authorities has been that sticky inflation has been accompanied by discernible slack in the labour market, consistent with the level of GDP still 7% below its pre-pandemic path. The oil shock accentuates this dilemma by simultaneously pushing up inflation and pushing down growth.

How, then, should policy respond? Arguably, monetary policy should look through temporary supply shocks. But what if the adverse supply shock remains persistent, simply morphing from one form to another – a supply shock from COVID-19 for two years replaced by oil prices remaining elevated for a while? The concern, in our view, comes down to inflation expectations. Sticky headline CPI over the last two years has meant that both household and business inflation expectations – notwithstanding some recent softening of household expectations– have hardened discernibly over the last 18 months (Figure 6). This is tantamount to the Philips Curve shifting up and creating a much more unfavourable trade-off between slack and prices for monetary authorities down the line.

Figure 7: Inflation Expectations (1-Year Ahead)

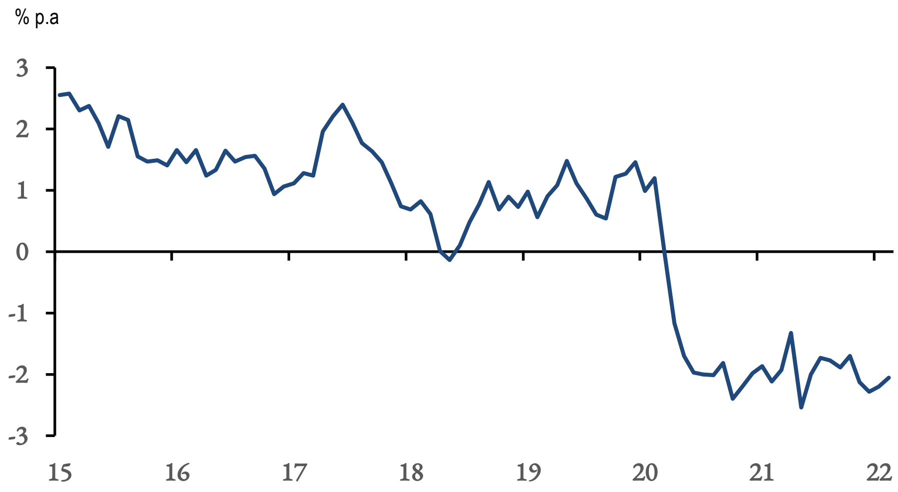


Source: RBI, IIM Ahmedabad survey

Given the juxtaposition of slack, sticky headline and core inflation, and firming inflation expectations, we have therefore previously argued that monetary and fiscal policy, which reinforced each other in the throes of the pandemic, will now have to evolve from being complements to substitutes. (Chinoy, 2022).

Even as fiscal policy – better suited to offering targeted support amidst an uneven recovery – tries to remain relatively accommodative, monetary policy should gradually begin to normalise off very accommodative starting points (Figure 7).

Figure 8: Real Policy Rate



Deflated via core-core inflation; Source: MoSPI, J.P. Morgan

3. Fiscal Policy

Fiscal policy will confront its own trade-offs. To be sure, the February Budget created buffers to guard against shocks by making very conservative tax assumption for 2022-23. Even net of excise duties – which were budgeted lower on account of the November tax cuts – gross taxes were budgeted 0.5% of GDP lower in FY23 than the expected outturn in FY22 (Table 2). As a consequence, even if much of the remaining under-recovery from oil at $100/barrel is absorbed on the budget through further excise duty cuts, a tax buoyancy of about 1 on the non-excise tax component would be enough to bring total tax revenues to budgeted levels. So, budgeted tax receipts could be met, and budgeted expenditures protected, even if more of the oil shock is absorbed on the budget.

But several caveats exist. First, if crude prices climb even higher and/or the fertiliser subsidy increases, pressure on budgeted expenditures will emerge. Second, to the extent that higher oil prices are symptomatic of elevated global uncertainty and corresponding pressure on asset prices, budgeted asset sale revenues could be harder to pull-off such that the revenue implications go beyond the excise duty cuts.

Third, even if budgeted tax and expenditure targets are met, one shouldn't lose sight of opportunity costs. With the deficit pegged at 6.4% of GDP for FY23, absent the oil shock, higher-than-budgeted revenues would have presumably translated into higher-than-budgeted expenditures – an expectation likely baked into growth forecasts for 2022-23. In the wake of the oil shock, if revenue constraints preclude these extra expenditures from taking place, there would still be foregone growth cost, especially if capital expenditures with their higher growth multipliers come under pressure.

	FY20	FY21	FY22RE	FY22JPM	FY23B
Net Tax Revenues	6.8	7.2	7.6	8.0	7.5
Gross Taxes	10.0	10.2	10.8	11.4	10.7
Gross Taxes ex excise	*8.8*	*8.3*	*9.1*	*9.9*	*9.4*
Non-tax Revenues	1.6	1.0	1.4	1.4	1.0
Total Receipts	8.7	8.5	9.4	9.6	8.9
Revenue Expenditure	11.7	15.6	13.6	13.6	12.4
Interest	3.0	3.4	3.5	3.5	3.6
Subsidies	1.3	3.8	2.1	2.1	1.4
R.Exp (x int,sub)	7.4	8.3	8.0	8.0	7.4
Capital Expenditure	1.7	2.2	2.6	2.6	2.9
Total Expenditure	13.4	17.7	16.2	16.2	15.3
Fiscal Deficit	-4.7	-9.2	-6.9	-6.6	-6.4
Nominal GDP growth	6.2	-1.4	17.2	17.2	11.1

Source: Budget Docs, J.P. Morgan

More generally, the greater the oil shock absorbed on the budget, the larger the hit to demand and growth, because of the higher marginal propensity to spend off the fiscal vis-a-vis the private sector. This is not to suggest that policymakers should not consider any excise duty cuts, because higher retail prices could further harden inflationary expectations, increasing the challenges for monetary policy. However, when considering fuel tax cuts, these trade-offs will need to be recognised.

Finally, policymakers could always cut duties, not cut spending, and let the deficit widen commensurately – effectively pushing out some of the ToT costs to the future in the form of higher debt – but negative surprises on the fiscal during periods of heightened macro uncertainty and at a time when India's gross borrowing is already seen as being hefty could generate significant risk premia in markets.

All told, the fiscal will confront several trade-offs and should try to engage in burden sharing and avoid corner solutions. What is clear to us, however, is that as soon as markets begin to stabilise, authorities must plough ahead with planned asset sales/disinvestments to create much-needed fiscal headroom, without trying to perfectly time the market. This will allow the fiscal to protect expenditures even as it takes on some of the oil shock on the Budget.[7]

A persistent adverse supply shock is complicated and challenging to respond to, and the new equilibrium will inevitably need some combination of a weaker rupee, higher rates, and judicious fiscal management. Beyond the very near term, however, we believe policymakers must consider systematically hedging crude price imports in global markets to protect the economy from periods of outsized volatility, apart from the medium-term objective of reducing dependence on imported crude.

References

Anand, Ding and Tulin (2014). Food Inflation in India: The Role for Monetary Policy IMF Working Paper (WP/14/178)

Bernanke, Gertler and Watson (2004). Oil Shocks and Aggregate Macroeconomic Behavior: The Role of Monetary Policy, Journal of Money, Credit and Banking, 36,2

Bernanke, Gertler and Watson (1997). Systematic Monetary Policy and the effects of Oil price Shock, Brookings Papers on Economic Activity, 91-116

Cecchetti and Moessner (2008) Commodity Prices and Inflation Dynamics, BIS quarterly review

Chinoy (January, 2022): The Fiscal-Monetary Tango, Business Standard

Chinoy and Jain (2021a) COVID-19 and India's Macro Economy: Pre-Existing Conditions, Performance and Prospects, Indian Policy Forum, 2021

Chinoy and Jain (2021b) Fiscal Policy and Growth in a Post-COVID-19 World, Economic and Political Weekly, February 2021

Chinoy and Jain (2018) What Drives India's Exports and What Explains the Recent Slowdown? New Evidence and Policy Implications, Indian Policy Forum, 2018

Chinoy and Jain (October, 2015). Oil and the Indian Economy: Where did the Windfall Go?, J.P. Morgan Research Note, 2015

Garganas, Nicholas (2006) Speech on Macroeconomic management in an environment of aggregate supply shock, BIS Review

Hsing (2010) Test of the Marshall–Lerner Condition for Eight Selected Asian Countries and Policy Implications, Global Economic Review, 39:1, 91-98

Johnson, H.G. (1958). Towards a general theory of the balance of payments, International Trade and Economic Growth (pp. 153-68).

Rassi and Tulin (2015), Price and Income Elasticity of Indian Exports —The Role of Supply-Side Bottlenecks, IMF Working Paper (WP/15/161)

Woodford (2003) Interest and Prices. Foundation of a theory of Monetary Economics. Princeton University Press.

Notes

[1] Net of trade in defense equipment, for example, combined trade with Russia and Ukraine constitutes just 1% and 2% of India's export and import basket, respectively. Instead, the indirect trade channel through weaker European growth is likely to be more significant. India's exports to Europe constitute more than 14% of the export basket and European growth is likely to be meaningfully impacted by Russian-Ukraine conflict.

[2] Higher domestic prices should induce some behavioural impact in terms of lower import volume growth, but that is likely to be a second-order impact.

[3] Because state duties are ad valorem, they would remain unchanged if retail prices remain unchanged. This is just a simplifying assumption. In actuality, we expect the hit to be shared between the Centre and some states.

[4] To be sure, the Budget had built in fiscal buffers to deal with shocks by budgeting revenues very conservatively. Absent the oil shock, therefore, tax revenues would have been higher than budgeted. With the fiscal deficit fixed, this would have meant higher expenditures/GDP than budgeted, implicitly baked into FY23 GDP forecasts. Post the oil shock, any cut in oil duties will mean expenditures – and therefore growth – will be lower than previously envisioned. Furthermore, to the extent that higher oil prices are symptomatic of elevated global uncertainty and asset prices, budgeted asset sale revenues could also remain under pressures, such that the revenue implications go beyond the excise duty cuts.

[5] To be sure, the household response to higher crude prices will depend on whether the shock is perceived to be temporary or permanent and/or whether liquidity constraints prevent households from smoothing consumption.

[6] Demand and utilization rates, rather than balance sheet effects, are currently the binding constraint on growth. Therefore, a surge in profits in the pandemic year did not translate into commensurate investment. Similarly, an income shock is unlikely to translate into a commensurate pull-pack in investment, making a marginal propensity to investment assumption of less than 1 plausible.

[7] To be sure, selling public sector assets is akin to increasing the economy's net debt (gross debt adjusted for public sector assets). That said, if asset sales are used to finance much-needed physical and social infrastructure with high economic returns, this is akin to a productivity-enhancing swap on the public sector's balance sheet that does not reduce net debt.

Indian Public Policy Review 2022, 3(2): 15-28

History and National Security#

Shivshankar Menon*

Abstract

This paper examines the links between the history we choose to tell ourselves and its implications for national security in India. It discusses history in the Indian tradition, the history that is current in India, some common current historical tropes, and why it matters. In the process it seeks to draw some real lessons of India's history for our national security.

Keywords: History, National Security, nationalism, India, victimhood

Publication Date: 18 March 2022

Adapted from remarks delivered at The Takshashila Institution, Bangalore, on 1 December 2021

* Shivshankar Menon is an ex-diplomat and has served as the National Security Advisor to the Prime Minister

There are worrisome national security implications of the present uses of history in India. The fact is that history has important social and political functions in every society. It is inextricably linked to contemporary politics – and therefore to national security. There is no such thing as pure history: objective and divorced from context, an academic discipline maintaining very high professional standards, in isolation in an ivory tower. The issue is the kind of history that we choose to tell ourselves — and teach our children — for it affects what we think and do, now and in the future.

I History in the Indian Tradition

Absolutely central to history in all traditions is the critical distinction between established fact and fiction: between historical statements based on evidence and subject to evidence, and those which are not.

Increasingly often today we see the politico-ideological abuse of history, not just in India but in several major countries. The past, or an *imagined* past, is used to justify religious fundamentalism, polarisation, and chauvinism. We laugh when we hear our neighbour speak of Harappa and Mohenjodaro as "four thousand years of Pakistan." After all, Pakistan was not even thought of before 1932-3, became a political slogan only in 1940, and came into existence only in 1947. Sadly, some of us in India are falling into the same anachronistic trap.

We have become used to politicians and other public figures speaking of things they are clearly ignorant about, mangling history and logic in statements such as: Einstein discovered gravity, Darwin was wrong because no one witnessed an ape turning into homo sapiens, Chandragupta defeated Alexander, India invented plastic surgery and in-vitro fertilisation procedures, Haldighati was a victory for Maharana Pratap, cow urine cures Covid, India achieved independence in 2014 not 1947, and so on.

One might ignore these statements or laugh at them if they were just reflections of ignorance or jokes. Sadly, they are more. They are part of a larger narrative about our own history, grounded in an attitude of anti-intellectualism, that has the political effect of unsettling society. They also affect India's credibility as a nation, as a society, and as a power. Worse, they affect India's ability to function as a state and achieve the transformation of India. The foundation of successful public policy is evidence-based reliable knowledge, and high-frequency information. In its absence, we settle for policy-driven manufacture of evidence and history.

If asked why they do so, the purveyors of false or rhetorical history would probably say that it is necessary for the country, its unity and even for emotional satisfaction. All human beings and institutions need a past. Renan said that nations are historically novel entities pretending to have existed for a very long time (2018). Nationalist versions of history will therefore include omissions, inventions, and even, in extreme cases, lies. The problem is that history as fiction is now becoming widespread in India, encouraged by anti-intellectualism and a mindset that sees 'good history' simply as 'history that is good for our group/country /cause', and is spreading unchecked on social and mass media.

II The History We Tell Ourselves

History is like a map, an imperfect reflection of a larger objective reality, which, over time and with improvements in the historian's art, becomes clearer and more representative. That map is important to India's security policies because we act, choose and decide on the basis of the map of our own experiences, or history, that we carry in our heads. Perception matters; when perception does not match objective reality, policy errs or fails.

The broader problem is that we in India have been taught a version of our history which ignores how connected to the world India has been, and how our prosperity and security have been directly proportional to that linkage.[1] This may be because the regions which undertook these contacts with the rest of the world, what historians call coherent core areas — i.e., areas characterised by stable, long-term political and cultural institutions, like Bengal, Gujarat, and the Malabar and Coromandel coasts — have been ignored or downplayed in our historical narratives, in favour of the relatively insular Indo-Gangetic plain and the region around Delhi.

This was understandable when our history was being written by the British. They wrote a narrative that legitimised their rule, by making it a continuous sequence of empires, by stressing their alien nature and the role of foreign invaders, and by concentrating on polities near or based on Delhi. This saga of empires was periodised by religion, and caste was emphasised, disregarding the fact that other factors were always more important in practice, and that the ruling elite was always of mixed religious persuasion and origins.

One can understand why the British would prefer such a narrative, serving as it did to justify their own rule. What is one to make, however, of the fact that there are Indians who persist in these characterisations, complete with their narratives about religion and caste, accepting thereby the mythological history foisted on us by the British, despite having been shown by the best historians of the day that they are wrong?

Moving away from a Delhi-centric or Indo-Gangetic valley-centred view of Indian history and including the history of the other regions in our consideration gives us a very different historical legacy; one that should form an increasingly important element of our strategic culture and serve as a driver of our policy choices. If you look at Indian history as Delhi-centred, you will fall into the mistake of believing, as KM Panikkar did, that "India has, throughout history, had trouble arousing much interest in the world beyond its borders", which he contrasted to British attentiveness to developments around the Raj (Pannikar 1961). Instead, it is maritime Asia that has determined our prosperity and security to as great if not a greater extent than any trans-Himalayan expedition (Sivasundaram 2020).

Once one includes the history of southern and western India, as also Bengal and Orissa, in consideration, it becomes clear how strong India's trade, military and cultural links with the rest of the world have been, going back to 2,600 BCE. Ptolemy attests to this in the 2nd century CE; Pliny

---

[1] See, for instance, Asif, Manan Ahmed. 2020. *The Loss of Hindustan: The Invention of India.* Cambridge: Harvard University Press. pp. 1-27.

in the mid-1st century CE grumbles about gold and silver draining away to India from the Roman Empire for luxury goods – a problem that the British also had in the early days of trading with India, until they discovered the commercial uses of opium.

The reach and extent of the soft and hard power of non-Gangetic regions of India in both mainland and archipelagic south-east Asia is visible to this day in the great ruins of Angkor Wat and Borobudur, on the walls of the Vaikuntha Perumal temple in Kanchipuram, and in Hampi, and in the living culture of many countries who formed India's maritime neighbours. Chola activist external policies and willing militarism enabled them to last from the 3rd century BCE to the 13th century CE. Their example was actively followed by the Pandyan (6 century BCE to 12th century CE) and Pallava (3rd to 9th century CE) dynasties. The same is true of the reach and influence of Gangetic or Indus-valley-based political entities like the Mauryas or Kushanas, as the spread of Buddhism overland to the Pacific and the Mediterranean attest. The Mughals, for their part, played an active role in central Asian politics too. This is a strong and abiding legacy that many seem to have chosen to forget.

The history we tell ourselves influences the policies we choose or favour.

For instance, there were several Indian views on India's security and foreign policy just before independence. Within the establishment and the Congress, there were those who believed in a nationalist version of our history, including Nehru, and those who accepted the British version of Indian history as Panikkar did. There was, however, a tolerance for differing views. GS Bajpai's views on alignment were clearly very different from Nehru's, as were KPS Menon's views on China. Yet Nehru made one the first Secretary-General of the MEA and the other the first foreign secretary of India, his top civil servants in foreign affairs.

Panikkar, Bajpai, and Patel prioritised the fight against communism and India's role as a security provider in south-east Asia. To that end, Bajpai, Panikkar, Rajaji, and others were ready for India to work with Britain in Asia in a close defence partnership. Nehru, KPS Menon and others, on the other hand, prioritised decolonisation as a means to enable pan-Asian solidarity, leading to joint actions to preserve peace, in contrast to the traditional power politics of the US and western powers.

There was a "Hindu" alternative to the debate in the Congress and official circles – often called Hindu nationalism, albeit wrongly so, since all sides of the discussion involved Hindus, and all were nationalists. Swami Vivekananda had argued at the end of the nineteenth century that reformed Hinduism based on the early Vedas could liberate India and free the world from "fanaticism and religious wars". This, he believed, would involve karma-yoga, making ourselves physically strong and rebuilding Indian civilisation using modern ideas. Once India mastered science and became "a European society with Indian religion" (Vivekananda 1897), it would conquer its former conquerors, Muslim and Western, by spiritual rather than by military power.

The idea that India's security could be achieved by universal acknowledgement of the truths of Hindu sanatana dharma (roughly, the true, eternal way), later also drove the thinking of Savarkar and Golwalkar, who led the Rashtriya Swayamsevak Sangh, and is reflected in Narendra Modi's professed goal of India as a vishwaguru ('world teacher'). Savarkar and Golwalkar both argued that Hinduism is destined to bring world peace, but that sanatana dharma would only be taken seriously when India is a "self-confident, resurgent and mighty nation" (Golwalkar 1966). Theirs was, at that time, a small voice without influence or power, and was focused by its leaders on eliminating "internal threats" —

Muslims, Christians, and communists — in pursuit of which they were ready to work with the colonial power, while also admiring European fascists.

Let us consider four of the tropes about Indian history that are current today:

1. A thousand years of slavery

This is an ahistorical or anachronistic construct that may be useful for political mobilisation in post-Partition India but does not fit known and provable facts. Until British rule, the ruling elite in India was not constituted on religious lines, and always included people of different faiths, irrespective of the faith of the ruler. The British were the first elite group to resist assimilation into Indian culture, and to assert a racial basis for their rule and 'superiority.' Every other group that came into India became 'Indian', whatever that meant at that period and in the region they encountered. Hence the British insistence on hardening and stressing caste and religious divisions in the majority population so as to divide and rule.

Interestingly, it is the British colonial version of our own history that is now being replayed in the refrain of 1,000 years of slavery, of Muslims as foreigners, and in pushing a form of political Hinduism created in the last century. What is being attempted is to remake India and our sense of it into a late-19th century European nationalism, seeking a homogeneity of ethnicity, language, and religion, founded on social Darwinist ideas of race and superiority. It was this form of toxic nationalism that led Europe into four centuries of unremitting warfare, first among themselves and then against the rest of the world, culminating in two world wars that effectively destroyed Europe's power and role in the world. Is that where we want to take India?

Characterising the last 1,000 years as slavery is not borne out by the historical record. Until almost 1800, there was little to differentiate the development of western Europe from India, eastern Europe, or China (or, to be more precise, of portions of each of these regions) from one another. In these areas in India, living standards were similar to those in advanced parts of China and western Europe. Proto-industrialisation had taken place precisely in those areas of India that were most connected to the world through history— Bengal, Gujarat, the Malabar, and Coromandel coast — i.e., maritime India.

It was only later that the 'great divergence' (as it is now known) took place, with western Europe's economic and technical advancement in the industrial revolution creating a Europe-centred world. As Pomeranz says, "we cannot understand pre-1800 global conjunctures in terms of a Europe-centred world system; we have, instead, a polycentric world with no dominant centre." (Pomeranz 2000) Angus Maddison's estimates of GDP bear this out and show how late the great divergence actually took place (Bolt and Zanden 2020).

For our purposes, the figures below are interesting because they show what Empire did to once prosperous and advanced societies in Asia like India. If there is a period of Indian history that was characterised by slavery, it is that of colonialism in India, that is, the British empire. At least until today, we have not used that past to create a narrative of historical humiliation to justify present-day bad behaviour on the global stage, as the Chinese regime does. In India, the narrative of 1000 years of slavery is being used politically to divide and polarise a society already traumatised by Partition.

Distribution of Population & Income in World Economy, 1000-1820

	% Of World Population			% Of World GDP		
Year	**1000**	**1700**	**1820**	**1000**	**1700**	**1820**
Asia, *of which*	65.5	62.1	65.2	68.2	57.7	56.5
China	22.1	22.9	36.6	22.7	22.3	33.0
India	28.1	27.3	20.1	27.8	24.5	16.1
Western Europe	9.6	13.5	12.8	9.0	21.8	22.9

Source: (Nayyar 2013, 13)

2. India should not have taken Kashmir to the UN in 1948

There has been much second guessing of the decision to take the issue to the UN, and of the conduct of that war, including the decision to accept a UN-sponsored cease-fire in December 1948. Patel, for one, questioned Nehru's promise to the UN of a plebiscite or referendum to determine the future of Kashmir. Keep in mind, though, that Patel was initially ready to hand Kashmir over to Pakistan in return for Hyderabad. It was only after Pakistan sent in tribal raiders followed by the Pakistan Army that he changed his mind (Nandurkar 1976, 62). It was an evolving and very unclear situation, and one that should be evaluated in the context of its time. What is seldom asked is: what were the alternatives available to government at that time?

Hindsight is a wonderful thing, clear and certain, and never available to the participants. For the author, this story is proof of how limited the instruments and options available to India were at the time. The first Commanders-in-Chief of both the Indian and Pakistani armies were British. Rob Lockhart and Roy Bucher reported more extensively to their own diplomats and their compatriots in Pakistan than to their nominal masters (Advani 2013). In India, there were even occasions when the Commander-in-Chief of the Indian Army Gen. Roy Bucher did not carry out direct orders from his Indian political masters (Dixit 2002).

When the moment of decision came, it was the considered advice of the Indian and British military commanders to Nehru that the army could not carry the war to a victorious conclusion, and that India should therefore approach the UN and, later, accept the cease-fire. Lt. Gen. L.P. "Bogey" Sen later titled his account of the Kashmir confrontation 1947-48 'Slender was the Thread,' which gives you an idea of how close India came to losing Kashmir (Sen 1969).

At that time there was no doubt and ample proof of aggression. Nonetheless, at the UN, the UK led the US into treating the matter as a dispute between two states over the status of J&K rather than as a case of aggression that must be vacated. Their aim was both to use Pakistan, and to insert themselves into the issue. The prevarication and diplomacy involved is well described in Chandrashekhar Dasgupta's book, which is an excellent description of the issue itself, as also of how power politics is played (2002). To assert, with the benefit of hindsight, what ought to have been done then is a leap in judgment.

3. India should have intervened to make Tibet independent in 1950

As India approached independence, it had been clear for some years that China intended to occupy Tibet. Mao had listed Tibet among the lost territories of China in 1936 (when he included Nepal and Bhutan as well). While sitting in the western hills outside Peking in 1949 from April to September, he had listed the "liberation of Taiwan and Tibet" among the first tasks of his new government (Menon 2021, 56). Nehru and his officials were aware that this would be an adverse change in the situation on our borders. They therefore initiated contacts with the Tibetan government of the Dalai Lama to see what might be done and got the military options examined internally from 1948-50. An Indian Army major, Zorawar Chand Bakshi, was sent into Tibet to report to Foreign Secretary KPS Menon about the situation and possibilities. He found that the Dalai Lama was a minor and that the Tibetans themselves were completely divided. Apart from Shakabpa and Tsarong, the rest of the Kashag did not want to provoke the Chinese by a military build-up (ibid).

When the Tibetans did manage to ask for arms from India and sent a delegation to canvas the world, it was a case of 'too little, too late'. India did supply some weapons in June 1949 and did try some military training. But as India's Chief of the Army Staff (COAS) General Cariappa told Nehru in October 1950, the Tibetans had no military capacity to withstand the battle-hardened PLA (who had just driven the Kuomintang (KMT) off the Chinese mainland). The COAS added that the Indian Army itself, engaged in war in Kashmir and in internal security duties, could at best spare one battalion of troops for Tibet, that they would not be acclimatised, and would have to be deployed at Yatung in the Chumbi valley or, at the limit, no further than Gyantse, even that not for long. In effect, India had no real military options to defend Tibet (ibid, 57).

Nehru, therefore, had no choice but military inaction and the use of diplomacy and persuasion. And in that too he was inhibited both by what the British had done to promote and recognise Chinese suzerainty over Tibet (which they presented as a step to keep the Russians out of Tibet), and by the Tibetan desire to negotiate directly with China. There had been a consistent British refusal to arm the Tibetans in the past, and in 1940 a British Foreign Office note said presciently that "China is bound to absorb Tibet after the war if not before and we can do nothing to prevent it" (ibid, 57). The US tried to get the Dalai Lama to leave Tibet in 1951 for exile in Thailand or Sri Lanka but the Dalai Lama chose not to accept the offer. (Mao had offered better terms and the Tibetans were divided.) (Kalha 2014)

Nehru is maligned for 'losing' Tibet in 1950. But he had no option to intervene effectively. In fact, he had no military choices and little diplomatic play. The signing of the 17 Point Agreement for the Peaceful Liberation of Tibet on 23 May 1951 between the Tibetan authorities and the PRC further limited India's options. Incidentally, this remains the only such agreement in PRC history, and its signature implicitly recognises de facto Tibetan independence and Tibet's status as different from the rest of China before 1950. It has been repudiated by the Dalai Lama.

On November 18, 1950, Nehru wrote in an internal MEA note: "It must be remembered that neither the UK nor the USA, nor indeed any other power, is particularly interested in Tibet or the future of that country. What they are interested in is embarrassing China" (Krishna 2007, 230-237).

Sadly, this is as true today as when Nehru wrote it. When the Tibetans appealed to the UN on November 7, 1950, they got no support worth the name.

4. India won the war but lost the peace in 1971

Did India really lose at the peace table what it won in the war of 1971? In July 1972, Mrs. Gandhi and Zulfikar Ali Bhutto (who had become Prime Minister of Pakistan) met to discuss the peace. The Simla Agreement of July 2, 1972 provided for India to vacate all west Pakistani territories occupied during the war, and to release all Pakistani prisoners of war. It was agreed to redraw and adjust the CFL of 1948 and call the new line the "line of control" (LoC) and to settle India-Pakistan issues bilaterally.

The conventional wisdom, supported by an account that PN Dhar wrote thirty years later, is that Mrs. Gandhi was keen to settle the Kashmir issue but was fooled by Bhutto (Dhar 2001). Bhutto agreed that the problem be resolved by Pakistan keeping what was west of the LoC and India east, but didn't want this in the formal agreement, fearing the reaction of the Pakistan Army at home to what they would call an abject surrender. This private understanding on a future settlement of J&K was therefore left to be formalised publicly later. Bhutto is said to have fooled Mrs Gandhi since he never had any intention of keeping his word and got an Indian promise to return all territory in the West and the prisoners of war.

It is true that India proceeded from the sense that an imposed peace – something in the nature of the Versailles accord that ended World War I – would only create resentment, unite Pakistan, and sow the seeds of another war soon. PN Haksar, Mrs. Gandhi's influential principal secretary, argued this forcefully in his notes to her. But what the received and commonly believed version ignores is the absence of any contemporary proof of a desire on Mrs. Gandhi's part to settle Kashmir on these lines, apart from PN Dhar's subsequent memory.

Indeed, not a single Indian draft before or during the Simla meeting included any such indication. Instead, India concentrated on insisting that the Kashmir and other issues be settled bilaterally by India and Pakistan, which Bhutto did commit to, thus taking Kashmir away from the UN for almost fifty years, until Article 370 was read down in August 2019. What is available on the internal record is Mrs. Gandhi saying that the country would not understand or forgive her if, after the victory on the battlefield, she gave away Pakistan Occupied Kashmir to Pakistan. One can understand Bhutto wanting to be seen as a hero at home and spreading the myth that he had fooled Mrs. Gandhi. It is hard to see why an Indian audience should believe it (Chandrashekhar Dasgupta 2021, 227-240).

Even if there had been some understanding at Simla on a Kashmir settlement, what realism would lead one to expect came to pass soon. Bhutto ramped up the rhetoric on Kashmir soon after returning to Pakistan. In any case, by 1975 neither Mrs. Gandhi nor Bhutto had the political capital at home to make the LoC the permanent international boundary between India and Pakistan. It seems doubtful that Mrs. Gandhi, the supreme realist, would expect any informal agreement with a Bhutto she did not trust to work.

Rather, and again realistically, she took what was available at Simla, which was a great deal better than what had gone before in India-Pakistan relations. Pakistan was broken, the subcontinent's political geography improved from an Indian point of view, and the Kashmir issue was bilateralised (Bhasin 2018, 231-251). In hindsight, the Simla agreement brought stability to the subcontinent for several decades. Even her fiercest critics at the time, Jayaprakash Narayan and Rajaji, praised her for the achievement of the Simla Agreement (Ankit 2022; Gandhi 2010).

It remains hard to see how a settlement of J&K that legalised the status quo would have been politically accepted in either country — in a Pakistan smarting from defeat, when large portions of the populace and army sought revenge from India, or for that matter in a triumphal India. It is also moot whether such a settlement of J&K would have lasted, given that it would have left both sides dissatisfied, and in all likelihood would have fallen victim to the fractious turn that domestic politics took soon thereafter in both countries. But this is speculation. What is certain is that, on balance, the Simla agreement brought stability and helped to avert a conventional war in the subcontinent for many years.

The subcontinent continues to this day to live with some baleful aftereffects of the 1971 war. Pakistan's realisation that J&K could not be taken by conventional war led to the pursuit of nuclear weapons and increasing reliance on terrorism and other asymmetric means. Bhutto and the Pakistan Army decided at Multan in 1972 to build nuclear weapons, "even if we have to eat grass", as Bhutto said. The conflicts over Siachen and Kargil are collateral effects of the Line of Control drawn after the 1971 war. Pakistan's stoking of insurgency in Kashmir and other parts of India, and Bangladesh's deep political divides and fissures are among legacies of the war with which we are still coming to terms.

But taken together India achieved all her war aims on the field and at Simla: the birth of Bangladesh, the bilateralisation of our disputes with Pakistan, the removal of a UN role, the cutting of Pakistan down to size, remaking the geopolitics of the subcontinent, and several years of peace with Pakistan. These are not small matters, and we reap the benefits to this day, the fiftieth anniversary of the birth of Bangladesh, in the relationship we enjoy with Bangladesh and its direct contributions to our security.

III. Why it Matters: The Real Lessons of our History for National Security

Why rake up these controversies about old times? Because they are being used for contemporary political purposes, and to manipulate what the average Indian thinks, by those whose history is neither evidence nor fact based. Ahistorical or fact-free stories like these affect our view of ourselves, and our capability to think rationally, to think big, and to be ambitious for India.

This matters at the level of both principle and practice. The reason leaders seldom lie to their international counterparts but find it easier to lie to their own people is because they are easily found out and because credibility is essential in dealings with those who are not under your control or authority. Pervasive lying creates a poisonous culture of dishonesty within a society (Mearsheimer 2011, 90-101). Internationally, lying by leaders and the backlash it provokes affects their ability to pursue effective external and security policies.

Bad history makes bad policy. Indeed, history shows how bad history was used to justify bad policies. Bad policy leads to bad results. This is all the more tragic for a country where there is much to learn and adapt from history, properly studied. In this final section, let us consider five lessons of

India's unique history, each of which, in the author's view, has implications for our national security calculus.

1. Self-strengthening and strategic autonomy

India has a unique endowment of geography, history, economic resources, demography and other long-term drivers. Therefore, India cannot just imitate anyone else, like China or the US, though it must learn from their experience. No other country shares India's interests to the point of being invested enough in India's security and territorial integrity to defend it. This is even more so now that India is a 'rising power'. Self-strengthening and a grand strategy of autonomy are therefore essential and unavoidable.

In practical policy terms, this results in hedging, balancing, resilience, using India's scale and strength. This also means that internal security is not distinct from external security. A mess up in one affects the other. Historically, in 1965, this dynamic worked for India in Kashmir. Internal cohesion matters.

Civil-military relations also need careful handling: consider the recent news of "Bhagavad-Gita's relevance in today's military leadership" allotted at a military command course (News18.com 2021). The Pandavas were armed with more than the Bhagavad Gita. They learnt martial skills from Drona before going to war and possessed the most advanced weapons of their time. Consider the PLA, a political army since its inception, which asks the question: Can ideological purity and revolutionary spirit defeat a carrier strike group? And their answer is a clear 'NO.'

The Indian Army is not and should not be a political army, though there are disturbing signs of its use in domestic politics and of military leaders making statements that suggest a political orientation. If it were to change its character, the Indian Army would lose the public respect and esteem in which it is held, as has happened to the police in India.

2. India is most prosperous and secure when most engaged and connected to the outside world

The historical record is clear. In today's situation, India's needs can only be met by engaging abroad. Almost half of India's GDP is the external sector. Imports are critical to our growth and transformation. 80% of India's imports today are maintenance imports, hard to do without—oil, coal, fertiliser, moong dal, non-ferrous metals, technology, and capital goods. And to pay for those imports, exports are a necessity.

Besides, one cannot walk on one leg; seeking active political and security involvement with the outside world while turning one's back on them, as it were, in economic terms. Walking out of RCEP, raising tariffs for four years, and if *atmanirbhartha* means a return to the import substitution days of the sixties and seventies – none of these help India's case for closer external engagement. If we need balancing coalitions with Japan, Vietnam, Indonesia, Australia, Singapore, and others to counter China's rise, we cannot have a one-sided or uni-dimensional relationship.

3. We are a maritime subcontinent with a continental problem:

India is a classic land-sea power – historically, it has been a maritime subcontinent with a continental problem. Today, the balance of forces in the seas around India creates an opportunity that does not exist on land. In this situation, the sea is the axis for India to project power, and essential for India's prosperity.

India's major security challenges are on the Asian continent—especially after Partition and the rise of China have physically cut off the traditional arenas of inner, central and west Asia. The world's largest boundary dispute with China, and Pakistan's inveterate hostility, mean that India cannot act like the other members of the Quad, who are islands in geopolitical terms.

India's tactical and operational problems on land cannot be solved at sea. The answer to Chinese salami-slicing on the LAC cannot be blockading the Malacca strait, or, for that matter, nuclear weapons. Each of these domains and portions of the spectrum of conflict needs to be dealt with on its own terms. In a larger strategic sense, of course, Indian strategic autonomy on the continent is instrumental for the success of a "free and open Indo-Pacific (FOIP)." Thus, India needs to have stronger partnerships with Russia and Iran for the continent; at the same time, a Quad and FOIP strategy for the maritime arena.

4. Not all problems are historical; look forward not back:

Economic and military strength and internal cohesion are essential for strategic autonomy. Image polishing, or control of the narrative, can take one only so far. As India's former Foreign Secretary Venkateswaran said when Rajiv Gandhi wanted MEA to improve India's image abroad, 'the image cannot be better than the original.' (Panneerselvan 2021)

The relationship with China is India's greatest challenge; It became a challenge after 1950 when China occupied Tibet. History, therefore, offers little help and limited guidance – certainly little that can be applied directly. The present day challenge is rooted in India's growing power imbalance with China, and can only be solved by looking towards the future, not to history.

5. Successful rising powers have followed similar strategies in the past:

There are two broad strands to the strategies followed by successful rising powers in the past.

One is to initially follow an accommodational strategy, working with the established order, norms, and hegemon(s) for as long as possible, while steadily continuing to accumulate the material basis of national power, namely military and economic power, or hard power.

The other is to develop a narrative to explain and propel one's soft power, both internally and externally. These narratives reconcile their growing power with the existing international order, acknowledge existing norms, and explain the purpose of their rise in terms acceptable to established powers. Ideally, if it is to be credible, this narrative should be the same both within the country and internationally.

It is only after the accumulation of sufficient power that rising powers have turned to shaping the regional or global order to suit their interests, as they see them.

No country has become a great power by wallowing in victimhood, dividing its people, picking fights with its neighbours and other powers on ideological grounds, or by parading an inferiority complex as history.

IV Conclusion

What we need in India is a forward-looking, confident India, not one that manufactures a history of victimhood for itself. Remember that the uprising of 1857 which looked backward failed; the freedom movement looked forward to transforming India and succeeded. 1857 was followed by a generation of great leaders and thinkers, most born between 1850 and 1875, from whom India could learn lessons of complete independence, economic emancipation, and social unity, for the political, economic, and cultural revival of India.

That is what we need to build the strong, prosperous, and modern India of our dreams.

References

Advani, Lal Krishna. 2013. "How Britain sought to thwart J&K's accession to India." *The Times of India*. November 11, 2013. https://timesofindia.indiatimes.com/blogs/lkadvanis-blog/how-britain-sought-to-thwart-j-k-s-accession-to-india/

Ankit, Rakesh. 2022. "Jayaprakash Narayan and Indira Gandhi, 1966–74: Before the Rivalry." *Studies in History 37, no. 2*: 213-234. https://doi.org/10.1177/02576430211069160

Asif, Manan Ahmed. 2020. *The Loss of Hindustan: The Invention of India.* Cambridge: Harvard University Press.

Bhasin, Avtar Singh. 2018. *India and Pakistan; Neighbours at Odds*. New Delhi: Bloomsbury.

Bolt, Jutta and Jan Luiten van Zanden. 2020. "Maddison style estimates of the evolution of the world economy. A new 2020 update". https://www.rug.nl/ggdc/historicaldevelopment/maddison/publications/wp15.pdf

Dasgupta, Chandrashekhar. 2002. *War and Diplomacy in Kashmir 1947-48*. New Delhi: Sage Publications.

Dasgupta, Chandrashekhar. 2021. *Indian and the Bangladesh Liberation War; The Definitive Story*. New Delhi: Juggernaut.

Dhar, P.N. 2001. *Indira Gandhi, the 'Emergency', and Indian Democracy*. New Delhi: Oxford University Press.

Dixit, J.N. 2002. *India and Pakistan in War and Peace*. London: Routledge

Gandhi, Rajmohan. 2010. *Rajaji: A Life*. London: Penguin.

Golwalkar, Madhavrao Sadashivrao. 1966. *Bunch of Thoughts*. Available online from https://www.thehinducentre.com/multimedia/archive/02486/Bunch_of_Thoughts_2486072a.pdf

Kalha, Ranjit Singh. 2014. *India-China Boundary Issues; Quest for Settlement*. New Delhi: Pentagon Press.

Krishna, B. 2007. *India's Bismarck, Sardar Vallabhbhai Patel*. Mumbai: Indus Source Books.

Mearsheimer, John. 2011. *Why Leaders Lie; The Truth about Lying in International Politics.* New York: Duckworth Overlook.

Menon, S. 2021. *India and Asian Geopolitics: The Past, Present*. Washington, D.C.: Brookings Institution Press.

Nandurkar, G.M. 1976. *Sardar Patel: Birth centenary, Volume 2*. Ahmedabad: Sardar Vallabhbhai Patel Smarak Bhavan.

Nayyar, Deepak. 2013. *Catch Up: Developing Countries in the World Economy*. New York: Oxford University Press.

News18.com. 2021. "Kautilya's Arthashastra, Bhagavad Gita May Soon Be Part of India's Military Training." September 03, 2021, https://www.news18.com/news/india/study-suggests-ways-to-integrate-lessons-from-arthashastra-gita-in-indias-military-training-4159601.html

Panneerselvan, A.S. 2021. "Image cannot be better than reality." *The Hindu*. May 03, 2021. https://www.thehindu.com/opinion/Readers-Editor/image-cannot-be-better-than-reality/article34465555.ece

Pannikar, Kavalam Madhava. 1961. "Speech to Indian School of International Studies." International Studies 22, no. 3 (July): 191-197. https://doi.org/10.1177%2F0020881785022003002

Pomeranz, Kenneth. 2000. *The Great Divergence; China, Europe, and the Making of the Modern World Economy*. Princeton: Princeton University Press.

Renan, Ernest. 2018. *What is a nation?: and other political writings.* New York: Columbia University Press.

Sen, L.P. 1969. *Slender was the thread, Kashmir confrontation, 1947-48.* Bombay: Orient Longmans.

Sivasundaram, Sujit. 2020. *Waves Across the South; A New History of Revolution and Empire*. London: HarperCollins.

Vivekananda, Swami. 1897. "Raise the masses slowly up, raise them to equality". The Hindu, February 6, 1897. https://www.thehindu.com/news/national/raise-the-masses-slowly-up-raise-them-to-equality/article4299189.ece

Indian Public Policy Review 2022, 3(2): 29-42

Size of Government in Kerala: Bulging Department of Agriculture in a Decentralising Structure

D Narayana*

Abstract

Kerala has devolved a large number of functions, funds and functionaries to the local governments. The state reports the highest number of local government functionaries per 1000 population among the Indian states. Adhering to the principle of subsidiarity would suggest that line departments at the state level reduce in size. The paper analyses the size of the state government in terms of employment, and in particular examines the efficiency of the Department of Agriculture by comparing the number of employees per unit area under cultivation in Kerala with that in Karnataka and Telangana. The findings are that Kerala reports 86 percent higher number of total employees per lakh population compared to Karnataka and about 25 percent higher than that in Telanagana. As regards the Department of Agriculture, while in Kerala an employee attends to 141 hectares, it is five times that area at 778 hectares in Telangana and ten times that area at 1425 hectares in Karnataka. The proportion of drivers, typists and clerks in the department in Kerala is also high. Running revenue and fiscal deficits and facing fiscal stress year after year for the last twenty years, where salary accounts for over 30% of the total revenue receipts, the state can aim for rationalization of its administration in order to have more resources for capital spending.

Keywords: Government Size; Employment; Agriculture Department; Efficiency; Kerala; Decentralization

Publication Date: 18 March 2022

---

* D. Narayana, Ph D (Indian Statistical Institute, Kolkata) was the Director of Gulati Institute of Finance and Taxation (GIFT), Thiruvananthapuram between 2012-13 and 2016-19.

I Introduction

Kerala is widely mentioned as a success story during the first wave of COVID-19. The state drew strength from the presence of empowered local government institutions and community participation in its fight against the pandemic. These have emerged as frontline institutions in containing the disease and in alleviating distress caused to the poor and vulnerable. Substantial devolution of funds, functions, and functionaries to the local governments over the last 25 years has helped strengthen these institutions. For instance, over 10% of the state's revenue receipts are devolved to the local governments (RBI, 2020: 73).

Democratic decentralisation got a boost with people's planning campaign launched in 1996 with the express intent of demystifying and *debureaucratising* planning at the local level (emphasis added) (Harilal, 2013). Local governments are 'entrusted with the responsibilities of public administration such as preparing project documents and estimates (working groups), technical vetting and issuing technical sanction (TAG/ committee system), selecting beneficiaries (gram sabha), and executing work (beneficiary committees)' (Harilal, 2013: 56).

It is generally believed that local plans have fared well in the service sector and triggered some notable success stories in agriculture (Harilal, ibid.). In particular, local governments have enabled commendable achievements in public education and health in the state (Isaac and Frankie, 2021). However, the record has been poor in productive sectors. For instance, in agriculture, area under paddy declined from 4.7 lakh hectares to 2 lakh hectares and production from 9.5 lakh metric tons to 5.2 lakh metric tons over the last 25 years (Isaac and Frankie, ibid.).

The devolution of more than 26 functions to local governments in Kerala has necessitated the enhancement of the number of functionaries at that level. The total number of employees under the local governments increased from 29,980 in 1995-96 to 36,480 in 2020-21. This is besides the local level offices of the development departments -- such as schools, primary health centres, anganwadis, and Krishi Bhavans -- which have been devolved (Isaac and Frankie, 2021). As a result, Kerala (along with Tamil Nadu) reports the highest number of local government functionaries - more than 2 employees per 1000 population - among states in India (Narayana, 2021).

According to the logic of subsidiarity, as functions are devolved to the local governments, one would expect the employee strength of line departments (i.e. at the state level) to fall, and the size of the state government to decrease. Kerala reports that more than 30% of the total revenue receipts (XV Finance Commission Report, Volume IV) go for paying salaries of employees, and a further 20% each for interest and pension payments. Under such fiscal stress, it is of interest to analyse the employee strength of the government and its efficiency. This paper takes up the issue of size of government in Kerala, and in particular, that of the department of agriculture, as the sector has been declining for the last three decades. In Kerala, the Agriculture department attends to only part of the sector, as a large proportion of the area under tree crops (such as natural rubber) is attended to by central government agencies.

The paper is organized in seven sections. Section 2 presents the relevant literature on size of government. Section 3 analyses distinct features of agriculture in Kerala. Section 4 examines the size and composition of government in Kerala in comparison with Karnataka and Telangana. Section 5 analyses the composition of the department of agriculture in the three states. Section 6 speculates on the possible factors behind the large number of drivers and staff in many departments. Section 7 concludes.

II Size of Government

Government is a vital institution in modern economic life although economists largely swear by the market. Much resource allocation takes place outside the market and consequently it is important, as succinctly put by Di Matteo (2013), to understand the appropriate size of government and its role in the economic life of its private citizens.

Size and growth of governments has remained an important subject of investigation since 1835 when Alexis de Tocqueville speculated on the subject. Wagner's (1883) well-known "law of increasing state activity" has spawned a vast literature on the subject. A new dimension was added to this debate by Peacock and Wiseman (1967) who argued that the rate of growth of public expenditure was driven by the desirable level of public spending and constrained by taxpayer perception of tolerable burden of taxation, and that this tolerance is greater during times of national or social crisis, which makes it possible to increase expenditures closer to the desired level.

As shown by Kliesen (2003), the 20th century saw a significant increase in the size and scope of government in the US because of two World Wars, economic depression of the 1930s, expansion of the welfare state in the 1960s and an upsurge in the environment regulations in the 1970s. Defense spending too has played an important role in boosting the size of the government. In countries with a federal structure of government, part of the increase was at the state and local level, as health and educational responsibilities of governments grew. The experience elsewhere in Europe and other OECD countries has not been different. Thus, governments have become large, multi-layered, and continue to grow in times of crises.

Measuring the size of government is complex as there is no single quantitative measure that conveniently summarises the role and functions of government. It is a producer of goods and services, an employer of labour and investor of capital. It also transfers resources, regulates individual and corporate activities, and incentivizes many market activities (Di Matteo, 2013). These functions are carried out by various levels of government depending upon the structure of government in each country. The size of government may be viewed from various angles. As stated by Di Matteo (2013): 'Two of the most common measures are government spending as a share of national output (GDP) and government revenues as a share of GDP. Other measures may include government spending per capita, the number of public sector employees, or public sector employment as a share of total employment' (p. 6).

Confining to the view of government by employment, three dimensions of it have become important. One is the sheer size in numbers, that is, the total employment in the various departments of government. Following Baumol (1966), the second dimension is the price of labour. And thirdly, the efficiency of providing service: 'The depth of government involvement in the economy gives rise to one common denominator for measuring government activity: is it efficient? Efficiency in government spending is a benefit that generates value for taxpayers, ensures that the costs of taxation and government intervention for economic growth and market performance are minimized, and demonstrates stewardship on the part of political leaders for their nation.' (Di Matteo, 2013: 5).

Local government efficiency has attracted some interest in recent years. A systematic review of the existing literature by Narbon-Perpina and Witte in 2018 identified 84 empirical studies on the subject. The countries covered range from many in Europe to Australia, Brazil and Chile in Latin America to Taiwan, Japan, Indonesia and Malaysia in Asia, Morocco and South Africa in Africa and the United States. India, with one of the largest numbers of local governments, does not find a mention in the survey. The studies measure local government efficiency using a wide variety of input and output variables. The selection of variables depended on the availability of data and the specific services the local governments must provide in each country. The output variables included by the studies range from aggregate of various municipal services in a global index to a set of specific local services. As regards input variables, mostly expenditure variables such as total expenditure, current expenditure, personnel expenditure, capital expenditure, and other financial expenditures are taken. Only a few studies have used number of local government employees as input.

Along with studies on the performance of local governments, there are studies on the size and efficiency of governments or departments. Recall that 'the greater the output for a given input or the lower the input for a given output, the more efficient the activity is' (Mandl et al., 2008: 3).

When specific outputs and outcomes could be measured, it is possible to conceive output per unit of input (whether money or personnel). What happens when outputs are not easy to measure, such as services provided by government? For a department like agriculture, efficiency may be measured in terms of the number of employees per unit area, or area normalized for crop combinations. For these ratios to be analytically useful, we have to either have some benchmarks in relation to which the performance can be assessed, or we have to place the observed ratios in a comparative frame. Here we have adopted the latter, where Kerala is compared with Karnataka and Telangana. A simple measure of number of employees per unit area is taken. The data used is from the staff appendix presented to the legislative assembly along with the state budget. It contains details of the number of employees by department and designation. It is a rich source of data, seldom used by researchers.

III The Plantation Crop-Centred Agriculture of Kerala

Among the three states Kerala is the smallest in terms of population as well as geographical area (Table 1). The population of Telangana is slightly larger than Kerala, and it has three times the area of Kerala. Karnataka has 83% more population than Kerala and almost five times its area. Further, Kerala has over a quarter of its geographical area under forests, compared to 23% in Telangana and 16% in Karnataka. All three states have about 12 to 13% of the geographical area not available for cultivation. Thus, the net cropped area in Kerala is around 20 lakh hectares, compared to over 40 lakh hectares in Telangana and 100 lakh hectares in Karnataka.

Table 1: Land Use Pattern in Karnataka, Kerala and Telangana

	Karnataka	Kerala	Telangana
Population(2011) (lakh)	610.95	334.06	350.04
Geographical Area(sq.km.)	191791	38863	112077
Land Use Types		Area (000 hectares)	
Forests	3073 (16.0%)	1081 (27.8%)	2540 (22.7%)
Not Available for Cultivation	2248 (11.8%)	538 (13.8%)	1492 (13.3%)
Net Area Sown	10044 (52.7%)	2043 (52.6%)	4377 (39.1%)
Net Cropped Area	10006	2016	4175
Gross Cropped Area (GCA)	12009	2584	4893

Source: First four items are from the Forest Survey of India, India State of Forest Report 2019, Ministry of Environment, Forest and Climate Change, Government of India.
Note: The data are for the year 2014-15. Items 5 and 6 are from the publications of the Directorate of Economics and Statistics of the respective state governments for 2016-17 or 2017-18.
Percentages shown are of the Reporting area which is different from the geographical area.

Kerala is one of India's largest producers of natural rubber, coconut, cardamom, and other plantation crops. These are tree crops (cardamom is a bush) with long life and not easily reversible -- once planted, the area cannot go back to field crops. As may be seen from Table 2, area under coffee and coconut is large in Karnataka as well; for every other tree crop, the area under the crop in Kerala is significantly more than in Karnataka. Telangana does not have any area under any of these crops, as the agro-ecological conditions of the state are not conducive for the cultivation of any of these crops. In total, the five crops listed in Table 2 account for close to 15 lakh hectares in Kerala and over nine lakh hectares in Karnataka. The share of plantation tree crops in the gross cropped area of the state is 57 % in Kerala, compared to 8% in Karnataka.

Table 2. Land under Plantation Tree Crops in Karnataka, Kerala and Telangana

Tree Crop	Area in Hectares		
	Karnataka	Kerala	Telangana
Tea	2,172	35,871	-
Coffee	2,45,288	84,976	-
Cardamom	14,629	39,080	-
Natural Rubber	55,000	5,51,050	-
Coconut	6,15,260	7,56,890	450
Total	9,32,349	14,67,687	450
% of Gross Cropped Area	7.76	56.81	0.009
GCA less Tree Crops	110,76,234	11,16,320	48,92,698

Source: indiacoffee.org; teaboard.gov.in; ecostat.telangana.gov.in; ecostate.kerala.gov.in; des.kar.nic.in.

In the case of each of the tree crop listed in Table 2, commodity boards support the cultivation, processing and trade of the crop. For instance, the Coffee Board of India is actively involved in the production and trading of coffee in India. It has a large extension wing spread over the coffee cultivating areas of Karnataka, Kerala and Tamil Nadu. The Joint Director of Extension in Kalpetta, under the overall supervision of the Director of Research, monitors and guides the extension activities of two Deputy Directors of Extension, eight liaison officers and 13 junior liaison officers in Kerala and Tamil Nadu. The extension wing of the Board is engaged in the supply of seed coffee to coffee growers, conducting village-level group meetings, and holding awareness campaigns and seminars on various aspects of coffee for the benefit of growers (Coffee Board of India).

There are organisations similar to Coffee Board for promoting the cultivation of tea, cardamom, coconut and natural rubber. The overall development of cardamom (small and large) is the responsibility of the Spices Board. The Coconut Development Board was established in 1981, with the specific objective of promoting coconut cultivation in non- traditional belts, rehabilitation of senile palms, integrated management of diseases and pests, and so on. Natural rubber has a board of seventy years' standing, which is one of the most integrated organisations dealing with rubber production, research, and exports.

Overall, Kerala has close to 60 % of its gross cropped area under plantation tree crops, which require very different support systems compared to field crops. In addition to the commodity boards for the development of tree crops, there are two directorates under the Ministry of Agriculture and Farmers Welfare entrusted with the development of crops in the country. The Directorate of Arecanut and Spices Development looks after the development of spices and arecanut (dasd.gov.in). The Directorate is responsible for spices such as pepper, ginger, turmeric, and nutmeg. Similar functions are carried out by the Directorate of Cashew and Cocoa Development. All these crops are cultivated in Kerala, and they account for about 2.3 lakh hectares of area (that is almost nine % of GCA in the state). Thus, commodity boards and directorates play a decisive role in the development of almost two-thirds of the GCA in the state.

In Kerala, the area under tree crops has more or less been maintained during the last ten years. While yield increases have varied among the crops, it may safely be said that production of these crops has not witnessed any significant fall during this period. Despite this, the share of agriculture in GSDP has witnessed a steep fall, as may be seen from Table 3. It is not unusual for agriculture, forestry, and fishing to see its share fall -- this has happened in all three states -- but Kerala has seen the largest drop in the share of crops sector in GSDP, of more than four percentage points in seven years. Clearly, the non-tree crop sector in Kerala is on a steep decline.

Table 3. Share of Agriculture in Gross State Domestic Product at Current Prices

Share in GSDP (%)	Karnataka		Kerala		Telangana	
	2012-13	2018-19	2011-12	2018-19	2011-12	2018-19
Crops	9.67	7.44	8.64	4.29	9.60	7.10
Livestock	2.44	2.39	3.35	3.25	5.60	6.80
Agriculture, Forestry & Fishing	14.90	10.97	14.39	10.67	16.3	14.8

Source: For Karnataka, Economic Survey, Various Issues available at des.karnataka.gov.in;
For Kerala, ecostat.kerala.gov.in; For Telangana, ecostat.telangana.gov.in

IV Size and Composition of Governments in Karnataka, Kerala and Telangana

Size of a government is here taken in terms of the number of employees. Table 4 presents data on total number of employees and their distribution by some major departments. The data are taken from the Staff Appendix presented along with the Budget each year.

There is little uniformity in the presentation of the information among the state governments. For the purpose of comparison of number of employees of a department across the three states the numbers had to be carefully aggregated. For instance, some states show the employees in the Department of State Goods and Services Tax and Department of Excise under Finance. So, Finance is taken to consist of Audit, Finance, Commercial Taxes, Small Savings and so on. Similarly, Department of Agriculture includes horticulture but not sericulture.

Table 4. Staff Strength under Some Major Departments in Karnataka, Kerala and Telangana, 2019-20

Department	Karnataka	Kerala	Telangana
Agriculture	7775	7903	6292
Animal Husbandry and Dairy Development	9584	8116	6323
Home & Transport	92826	72566	99548
Education	241765	224753	156008
Public Works	7689	8576	2966
Forest Ecology and Environment	8713	6762	6803
Water Resources	2544	7900	10566
Finance[$]	10226	15728	13413
Revenue	21759	24438	18375
Food and Civil Supplies	1357	2447	1349
Rural Development and Panchayati Raj	15475	11508	25646[&]
Social Welfare	12973	2973	15216
Labour and Skill Development	4678	2383	3060
Health and Family Welfare[#]	38,708	63,941	48,827
Total Number of Employees	512521	521531	440025

Source: Staff Appendix, Budget Papers available at http://finance.kerala.gov.in; http://finaance.karnataka.gov.in; http://finance.telangana.gov.in.

Notes:

[$] includes staff in the departments of commercial taxes, excise etc;

[&] includes Panchayat employees numbering 19,971;

[#] includes medical education.

It may be seen (Table 1) that Kerala is the smallest among the three states in terms of geographical area as well as population. But Kerala has the largest government in terms of employee strength. It is about 2% higher than that of Karnataka and 19 % higher than that of Telangana.

It is often said that the higher human development achievements of Kerala are owing to the larger government spending on health and education over a long stretch. So, one would expect a higher proportion of the total number of government employees contributed by these two sectors. While the bulk of the employee strength is contributed by these two departments in the three states, the share of these two departments in the total -- at 55 % for Kerala -- is higher than that for Telangana at 47 % but only equal to that for Karnataka (Table 5).

Table 5. Number of Employees per Unit Area and Population

State	Proportion in Health and Education (%)	Number per lakh Population	Number per 100 Square Km.
Karnataka	55	839	267
Kerala	55	1561	1342
Telangana	47	1257	393

Source: Author's calculations based on data in Tables 1 and 4

With the argument of larger number of employees in health and education sectors as a reason for the larger total number out of the way, let us take the number of employees per lakh population and per 100 square km. area. It may be seen that Kerala reports a much higher number compared to Karnataka and Telangana (Table 5). Kerala reports 86 % higher number of employees per lakh population compared to Karnataka and about 25 % higher than that in Telangana.

The primary function of the state governments in the Indian context is the provision of public services. Indicators such as the proportion of employees in the departments of health and education tell us the relative importance governments assign to these public services. In this respect Kerala is not very different from Karnataka. Note that the number of employees per lakh population does not tell us whether the citizens are under-served (in Karnataka) or over-served (in Kerala). Such an assessment would call for an analysis of the quantum of service provided in relation to the units requiring service. As the services provided by different departments are very different, this would call for a disaggregated analysis.

A first look at some of the departments suggests the following:

- In the Public Works Department, Kerala has 1000 more employees compared to Karnataka and almost three times the number in Telangana. Given that the geographical area of Kerala is significantly less than that in the other two states and that many functions and assets are devolved to the local governments, it is difficult to visualize that the requirement would be so much higher in Kerala.
- More or less similar conclusions may be drawn regarding the Forest Department. As presented in Table 1, the extent of forest area in Telangana is 2.5 times and in Karnataka three times that in Kerala. The size of the department in Kerala is almost equal to that in Telangana and about 77% of that in Karnataka.

- In the departments of Finance, Revenue, and Food and Civil Supplies, the employee strength in Kerala is more than that in Karnataka and Telangana. This contrast is most glaring in the Department of Food and Civil Supplies. If Telangana offers the services of food and civil supplies with 1349 employees, then why does Kerala require 2447? Almost double the population in Karnataka gets services of the department with close to half the number of employees of Kerala.

Turning to agriculture, a measure of the quantum of service provided may be taken as the area cultivated (it could be the number of cultivators, or a combination of area and number of cultivators and crop types and so on). As shown in Table 2, gross cropped area less tree crops receiving extension services from other organisations in Telangana is over four times and in Karnataka around ten times that in Kerala. Computing the GCA per employee in the department, it may be seen that while in Kerala an employee attends to 141 hectares, it is five times that number (778 hectares) in Telangana and ten times that number (1425 hectares) in Karnataka. An employee tending to just 1.4 square km. area looks very low by any standard. One is compelled to draw the inference that the agricultural department in Kerala is bloated.

Table 6. Total Number of Livestock during 20th Livestock Census 2019 (in 000)

State	Cattle	Buffalo	Sheep	Goat	Pig	Horses	Total Livestock
Karnataka	8459	2985	11051	6169	32384	7	29003
Kerala	1333	102	1	1359	104	-	2899
Telangana	4218	4226	19063	4935	178	4	32626

Source: Basic Animal Husbandry Statistics- 2019 available at dadf.gov.in

The picture is not much different in the animal husbandry and dairy development department. Table 6 presents the livestock numbers from the 20th Livestock Census of 2019. Both Karnataka and Telangana report livestock numbers ten times or higher than those of Kerala. If the number of cattle and buffalo are taken, it is over six times and eight times that of Kerala in Telangana and Karnataka respectively.

The number of employees in the department in Kerala is about 2000 more than in Telangana, and is only about 1000 less than that in Karnataka. Effectively these numbers suggest that while an employee in Kerala tends to 357 livestock numbers, employees are responsible for eight and fifteen times that number in Karnataka and Telangana respectively. If we take only cattle and buffalo, then while in Kerala an employee attends to 177 heads, it is 1194 in Karnataka and 1335 in Telangana.

Thus, a comparison with these two states in agriculture and animal husbandry gives us a perspective regarding the size of the departments in Kerala. The employee strength of the departments in Kerala does not bear a meaningful relationship to the area under crops, or the livestock numbers, or the performance of the sector in terms of their contribution to the GSDP of the state.

V. A Department of Clerks, Drivers and Mechanics

A department such as agriculture or horticulture entrusted with the primary responsibility of providing timely extension service and promote scientific agriculture is expected to have more technically qualified staff. In an era when information on soil and plant health, pests and diseases, land use etc. is accessed through satellites and other digital modes, where extension has acquired a new meaning, the department is expected to draw expertise from research institutions to interpret data and inform practices.

Across the three states, fairly high proportions of staff are directors and officers – 52 % in Karnataka, 59 % in Kerala and 63 % in Telangana (Table 7). These numbers suggest that Kerala is not very different from the other two states in this respect. But what is different is that while a director has around 16,930 hectares of GCA falling under their area of operation in both Telangana and Karnataka, it is 3017 hectares in Kerala -- only around 18 % of the area attended to by a director in Karnataka and Telangana. Similar differences may be observed with regard to the workload of officers as well – per capita area is 3280 hectares in Karnataka, 1328 hectares in Telangana, and only 261 hectares in Kerala.

Table 7. Staff Composition of the Department of Agriculture in Karnataka, Kerala and Telangana

	Category	Karnataka	Kerala	Telangana
1	Director-Joint, Additional, Assistant ...	**654**	370	289
2	Officers-Agriculture, Horticulture, Asst Agrl, Asst Horti, Agrl Extension ...	3377	**4271**	3684
3	Publicity Officer, Editor, Artist, ...	9	**17**	10
4	Engineer, Overseer, ...	20	**63**	5
5	Superintendent – grade I, II ...	**514**	375	81
6	Gardner / Mali	**539**	20	413
7	Research Assistant, Scientific Assistant, Technical Assistant, ...	-	**87**	-
8	Betel Picker, Binder, Helper ...	**30**	11	-
9	Driver – Senior, Grade I, II etc/ Cleaner	126	**340**	97
10	Borer, Fitter, Machinist, Mechanic ...	-	**214**	18
12	Duplicator, Dupl. Operator, ...	-	**62**	2
13	Clerk/Typist/Adm. Assistant/Confidential Assistant- all grades,	1394	**1544**	1191
14	Peon/Attender/ ...	**587**	302	147
15	Others*	**525**	227	355
16	Total	7775	**7903**	6292
	Officers/ Directors as a Proportion of Total (%)	51.85	58.72	**63.14**
	Sl Nos. 13 and 14 as a proportion of Total (%)	**25.47**	23.36	21.27
	Sl Nos. 7 to 14 as a proportion of Total (%)	27.49	**32.27**	23.12

Source: Same as Table 4.

Note: * includes Accountants of all grades, watchmen, soil chemists, lab attenders, tracers, draftsmen etc.

As regards the strength of other categories of employees, it may be seen that the departments in the three states have over a fifth of their employees falling in the categories of typists, clerks, assistants and peons of all grades. In this respect Kerala is no different from Karnataka; Telangana has a slightly lower proportion of such category of staff.

However, what is different is that when categories listed in Serial numbers 7 to 12 are added, the proportion rises to 32 % in Kerala compared to 27 % in Karnataka and 23 % in Telangana. There is a high load of drivers in Kerala, with almost one driver per director, compared to one driver for three directors in Telangana and for five directors in Karnataka. There is a similar high load of duplicating machine operators and mechanics in Kerala. Many of these categories have disappeared in other states but continue to remain in Kerala.

We may assess the need for drivers from a different angle, namely that of the geographical area to be covered for field visits. Taking measures like 'geographical area less forest area' to be covered per driver, it may be seen that in Karnataka a driver has to cover 1278 square kms., in Telangana 894 sq. kms., and in Kerala only 83 sq kms. As regards net cropped area, it becomes 794 sq kms in Karnataka, 430 in Telangana, and 59 in Kerala. If we apply the geographical area covered per driver in Telangana to Kerala, then Kerala would need only 31 drivers. If it is net cropped area, then the need would rise to 47. This would suggest that overstaffing of drivers in Kerala is of the order of 300. A similar computation done for the category of Directors and Officers of all types would suggest that around 80 % of them are surplus in Kerala.

We looked at the number of employees in different categories at an earlier time (2011-12) to see whether there has been any conscious effort to rationalise the staffing pattern. It is seen that while the number of superintendents and engineers has seen some reduction, the number of clerks/typists has hardly seen any reduction. The number of Directors has fallen by 30 but the number of officers has risen by close to 200. Most stunning is that the number of drivers has increased by 50 % during this period!

In sum, the characteristic of agriculture in Kerala is very different from that in the other two states. The area under field crops in the state is only around 40 % of the GCA, as the rest are plantation tree crops with their own systems of extension. The Department of Agriculture, which has the responsibility for less than 40 % of the net cropped area, is overstaffed to a very large extent and there has hardly been any effort at rationalising the workforce. It is also not very clear what the large number of clerks/typists, drivers, and mechanics in the Department do. Thus, Kerala -- acclaimed for the achievements of its local governments -- does poorly in terms of efficiency of its Department of Agriculture.

VI. Spoils of Power and Unionisation behind the Large Number of Drivers?

It is natural to ask the question, "why has there been such a large number of drivers in Kerala?" A definitive answer to the question would require a detailed examination of the issue which is not attempted here. Speculation on two possible factors may persuade researchers to take them up for rigorous analysis. The two factors that readily come to mind are, spoils system in coalition governments alternating every five years with thin majorities, and prevalence of unions affiliated to political parties in power. Two important pieces of evidence are offered in support of this argument.

It is well known that membership of state public service commissions, boards of state public sector enterprises, welfare funds and corporations are distributed among political parties and other interest groups to ensure their continued support to the governing coalition. Taking Public Service Commissions (PSC) of the three states, it may be seen that the Kerala PSC has 20 members, Karnataka 13, and Telangana 8 (in addition to the chairperson in each case). The ruling coalition in Kerala is made up of 11 political parties, whereas both Karnataka and Telangana are now ruled by single parties. Karnataka had a history of coalition politics in recent decades. The composition of the PSCs reflects this pattern.

When members are nominated by different political parties, they have to be treated on par, and the way this is done in Kerala is to offer official car with driver, staff, and other perquisites. The result is that Kerala PSC has 29 drivers on its rolls compared to five in Karnataka and only two in Telangana. Other staff are distributed similarly. In Kerala, there are 226 section officers, compared to 14 in Karnataka and 32 in Telangana. Number of stenographers and typists too are aplenty in Kerala PSC. In total, the staff strength of the Kerala PSC is 1784, compared to 225 in Karnataka and 166 in Telangana.

The total number of employees in government is not very different among the three states. Hence, the annual recruitment and the related workload cannot be very different in the three states. The increase in the number of PSC members (1.5 times as many as Karnataka, and more than twice as many as Telangana) and the eight-to-tenfold number of employees in the PSC can be seen as part of a spoils system. Ministries and departments too are distributed among the political parties of the coalition, who turn a blind eye to perquisites of officers and are often lenient with the unions affiliated to the coalition partners.

Examples of redundant worker groups continuing for years are also readily available. In recent years the use of road rollers by the Public Works Department has decreased, with the introduction of modern machinery by the contractors. The Government identified 140 posts of Roller drivers and 110 post of cleaners as surplus in 2003, and abolished 80 posts of drivers and 60 posts of cleaners. But as of October 2019, 26 drivers and 57 cleaners were still in their posts. They had hardly worked six days in *a year*. The Government did not explore the possibility of redeploying the idling crew despite several proposals being submitted by the Chief Engineer of Public Works Department (CAG, 2021: 49-50). It is possible that union pressure to not displace them was too strong. This example is comparable to that of borers, fitters and duplicators in the Department of Agriculture, noticed earlier (Table 7, row 10). In a unionised environment, numbers are strength, and efforts are made to protect them.

It may be fruitful to pursue an understanding of the higher number of employees in government in Kerala along these two directions, namely spoils system and unionisation. The few examples presented here suggest as much.

VII Conclusion

Following the 73rd Constitutional Amendment, village (Gram) Panchayats came into existence and have created participatory structures of grassroots democracy. The Panchayats are mandated to provide essential services such as drinking water, rural sanitation, preventive health etc., and are also agencies of the state for implementing schemes of Central and State governments. As per the Second Administrative Reforms Commission, 'agriculture, rural housing, watershed development, farm forestry and minor forest produce, rural electrification - all are functions [that] by their very nature "belong" to rural local bodies' (p. 34). While Article 243 G along with the Eleventh Schedule indicates the kind of functions to be discharged by the Panchayats, their assignment is left to the state governments by enacting enabling legislations. Kerala has been in the forefront of devolving functions, funds and functionaries to the local governments to make them more responsive, transparent, and accountable to citizens.

Subsidiarity is 'a principle that a central authority should have a subsidiary function, performing only those tasks which cannot be performed at a more local level' (Oxford Dictionary). In this scheme the citizen and the community are the centre of governance. Agriculture by its very nature is to be devolved to the Panchayats, and the state Department has only a subsidiary role. It is for the Panchayat to decide whether they need an office of the department, and if so, what functions it is to carry out. In Kerala, this question is all the more relevant and significant as over 60 % of the cropped area falls under tree crops, the development of which does not fall under the purview of the state's Department of Agriculture. In many Panchayats, this proportion would be significantly higher, making the Department largely irrelevant.

A government which spends over 60 % of its revenue receipts on salary and pension and runs huge revenue and fiscal deficits to run the government cannot afford to have departments such as the Department of Agriculture staffed so inefficiently. Especially difficult is the situation when massive floods (as in 2018) and pandemics (as in 2018 and 2020) necessitate funds for lifesaving, livelihoods, and reconstruction. These are over and above the funds needed for filling the infrastructure deficit, that has grown owing to insufficient and/or low quality capital spending over a long period. It is time the state examines many of its departments from the lens of subsidiarity, as it has striven to decentralise many functions earlier carried out by these departments.

References

Baumol, W J. and W G. Bowen. *Performing Arts-The Economic Dilemma.* Cambridge, Mass: Twentieth Century Fund, 1966.

Comptroller and Auditor General of India. *Report of the Comptroller and Auditor General of India on Economic Sector for the year ended March 2019, Government of Kerala, Report of the Year 2021.* https:// cag.gov.in/

Finance Commission of India. *XV Finance Commission Report Volume IV* 2020. https://fincomindia.nic.in/

Harilal, K N.. "Confronting bureaucratic capture: rethinking participatory planning methodology in Kerala." *Economic and Political Weekly*, 48(36), (2013): 52-60.

Isaac, T and R W. Franke. *People's Planning: Kerala, Local Democracy and Development.* New Delhi: Leftword Books, 2021.

Matteo, L D. *Measuring Government in the Twenty-first Century: An International Overview of the Size and Efficiency of Public Spending*, Fraser Institute, 2013. www.fraserinstitute.org

Mandl, U, A Dierx and F Ilzkovitz. *The effectiveness and efficiency of public spending* (No.301). Directorate General Economic and Financial Affairs (DG ECFIN), 2008.

Ministry of Personnel, Public Grievances and Pensions. *Second Administrative Reforms Commission: Reports*, 2006. https://www.darpg.gov.in/arc-reports

Narayana, D. "Good governance in Gram Panchayats of Kerala: Not so good?" in *Handbook of Decentralized Governance and Development in India*, edited by Rajasekhar D, 184-198. London: Routledge, 2021.

Narbón-Perpiñá, I., & De Witte, K. "Local governments' efficiency: a systematic literature review -part I". *International Transactions in Operational Research*, *25*(2), (2018): 431-468.

Peacock, A T., J Wiseman and J Veverka. *The growth of public expenditure in the United Kingdom (Vol.1).* London: George Allen & Unwin, 1967.

Reserve Bank of India. *State Finances a Study of Budgets of 2017-18 and 2018-19*, 2020.

https://rbidocs.rbi.org.in/rdocs/Publications/PDFs/0SF_271020FCF77451F1DF744B2B244875C785B8EF3.PDF

Wagner, Adolph. *Finanzwissenschaft.* Vol. 4. CF Winter, 1883.

Indian Public Policy Review 2022, 3(2): 43-57

Urban Governance in India and China: A Comparative View

Anil Kumar Vaddiraju*#

Abstract

The pace of urbanisation in India and China has, of late, been rapid. This raises concerns over urban governance in both countries. While urban governance in India is supposed to take place according to the 74th Amendment to the Constitution, in China, it is largely led, guided, and experimented upon by the Chinese Communist Party. With these aspects in view, this article looks at the extent to which urban governments in these countries have been moving from traditional government to network governance. What are the roles of state, civil society, and markets in the emerging scenario of urban governance so defined? The task of moving towards 'governance' is incomplete in both countries. While urban governance and urban civil societies are weak in India, markets are strong; whereas, in China, the urban government is strong while markets and civil society are weak. There is still a long way for both countries to go towards networked governance in urban areas.

Keywords: Urban governance, India, China, civil society, market reforms, governance, Karnataka, Telangana, Wuhan, Guangzhou

Publication Date: 18 March 2022

* The author is an Associate Professor in Political Science at the Institute for Social and Economic Change, Bangalore

I Introduction

India and China differ radically in their approaches to urban development and governance. Urban governance in China is *planned, incremental, and experimental,* primarily keeping in view economic growth. Urban growth and governance in India is *unplanned and left to the free-market, i.e. spontaneous and ad hoc.*

Social capital in governance does not appear, prima facie, to have much importance in China, since it is a Communist-party-led system of government, as it is in the governance of India's cities, which are governed by multiple political parties and afflicted by a diverse range of issues. A comparison of urban governance in these two giants makes for an interesting case study.

There are multiple paradigms of studying urban governance (da Cruz, Rode and Mc Quarrie 2018). This study focuses on social capital, civil society, and the transition from 'government to governance'.

Social capital theory envisages trust, cooperation, and social cohesion. It also envisages civic associations and civic engagement making governance more effective. However, in complex societies, social capital can operate in complex and even contradictory ways. That is, social capital can be used normatively for civic engagement and effective governance, as also for challenging the system and governance. In addition, there can be normatively 'bad' social capital and 'good' social capital. For example, extra-legal groups or mafia groups in urban agglomerations can exhibit considerable social capital — and that is bad social capital.

In studying urban governance, social capital theory has received mixed attention (Sullivan: 2009; Woolcock: 2011). In this paper, I am essentially interested in social capital contributing to effective and well-functioning governance. Further, in extremely divided and heterogeneous societies, ensuring social capital can lead to civic peace and social harmony. The article, however, does note that social capital challenging governments and social cohesiveness too can be critically important in certain circumstances.

Civil society, and the related concept of social capital, is essentially related to market societies. These concepts, however, are derived from the historical experience of Western societies (Metzger 2001), whereas the societies in question here are both Asian.

According to social and political theory, civil society is the space between the state and family (Vaddiraju 2014). In market or capitalist societies, this space is pervaded by market forces. However, in socialist, state-dominated societies, this space is problematic. In fact, the concept of civil society came to prominence globally, when the erstwhile state socialist societies collapsed in the Soviet Union. Therefore, in state-dominated societies, the space of civil society too is occupied by state and party organisations.

To what extent the space for market and civil society is available in socialist societies depends on how far the reform of state and markets has been carried out. In China, where the reform of socialism toward market society started in 1978 under Deng Xiaoping, limited space for market and market-related social organisations has emerged. On the other hand, in India, there are markets in urban areas, but not strong civil society to represent citizens. China represents a case of a strong state and weak civil society and markets. India, on the other hand, has strong markets but a weak state and weak civil society, failing to regulate its fast-emerging urban scenario.

Civil society and markets are also supposed to play a major role in the shift from traditional government to 'governance', wherein the vertical organisation of governing as a function of government shifts to horizontal partnerships between governmental institutions, civil society, and markets. This is sometimes known as network governance (Mathur 2008). The diagram below elucidates the conceptual framework employed in the paper.

Figure 1: The Conceptual Framework: The relationship between governance, institutions, markets, people, and social capital.

This paper deals with urban governance in India and China. Social diversity, social heterogeneity, and social hierarchy characterise India, whereas China seems to have a more homogeneous society. A comparison between India and China will also have to take note of the fact that India is a democratic polity characterised by a multi-party system, whereas China is a communist polity dominated by a single party, which largely takes all decisions. Thus, the social and political systems of these two countries are different, even though economic systems currently seem to allow for some comparison--particularly after opening up of China's markets. Keeping in view these differences, it is important to understand urbanisation and urban governance in both these countries.

Urbanisation in India is an actively debated topic, with two viewpoints being prominent. One is that it has been 'sluggish' (Kundu 2014); the opposite view is that the urbanisation process is more or less rapid. The first views posits urbanisation of the country at around 30%, proponents of the latter argue that nearly 50% of India is urban (Hashim 2020). However, both groups agree that of late the pace of urbanisation has increased. Another important fact, again accepted by both proponents, is that Indian urbanisation is 'top heavy' and 'exclusionary' (Kundu 2014), and that larger metros have been growing at a faster pace than smaller cities and towns[1].

The Chinese story appears to be different. China started its economic reforms in the 1980s, much before India; ever since the reforms, economic and urban growth have been rapid. Today, urbanisation in China is close to 50 per cent. The process of urbanisation in China is characterised by two precepts of Deng Xiaoping: 'Crossing the river by feeling for stepping stones' and 'Getting some regions and people richer first'. Economic and governance liberalisation has been carried out systematically, enabling some cities and urban social sections to get rich first. These regions have been largely those belonging to the Special Economic Zones situated in coastal regions (Mc Granahan *et al* 2014).

The Chinese system of registration, called the *hukou* system, has kept migration to urban areas restricted for rural workers. This system has been reformed over the years, and migration has been liberalised. However, older natives of urban areas, holding permanent residence in urban areas, continue to have an edge over those who work under the *hukou* system (Cai and Wang: 2010). That is, even after liberalising the *hukou* system, the *hukou* workers from rural areas who migrated to urban areas continue to be neglected and form the excluded population of Chinese cities. Even if less stringent, the *hukou* system continues, and we do not as yet know to what extent this creates problems for social capital in cities.

Urban local governments in China today have much more freedom to choose their policies of promotion of capital and labour, though the *hukou* system does make the urbanisation process in China exclusionary to some extent. The overall policy is guided according to the principles laid out by the central government. Such 'bringing capital and labour together' happens in a very unequal way: the system still gives priority to attracting capital to cities, whereas, in the ensuing process, the same priority does not seem to be given to migrant workers who form part of the *hukou* system.

Financially the ownership of township enterprises and greater devolution of finances and powers to cities make Chinese local governments stronger than their Indian counterparts. The Indian cities, particularly at the district level are deprived of the three 'F's –Finances, Functions, and Functionaries—that are constitutionally promised to them. Urban local bodies (ULBs) in India do not have ownership over any economic enterprises to make their finances viable. This results often in poor infrastructure and poorer service delivery in India cities. (Vishal, Singh, and Sridhar 2021) Therefore, the Chinese cities are better placed in terms of finances and powers than their Indian counterparts. In India the proposed reform of the property tax system to generate own resources by ULBs is yet to be done systematically and therefore, even though the cities have the potential for own resources, this potential is as yet unrealized.

Studies on civil society in China demonstrate (Howell 2011) that China being ruled by a single communist party, civil society and social capital have a chequered history. The state has generally dominated society till the 1980s. Reforms have led to an increase in civil society organisations in the 1980s. However, the Tiananmen Square incidents of 1989 saw the state tightening controls over civil society. Nevertheless, after the 1990s, civil society organisations have increased, and the fortunes of civil society are said to be fluctuating from time to time. The state itself has realised the importance of civil society organisations in Chinese society, which they envision as a path to greater state-society synergy and cooperation (Howell 2011).

In the following sections, I discuss the situation of urban governance in India, drawing on earlier published work (Vaddiraju 2013; Vaddiraju 2019). I then discuss the urban governance scenario in China, which draws from the published work of some Chinese and Western scholars (Sun and Lisaia 2018; Wu, Wan, and Jiang 2018; Mc Granahan *et al* 2014). The final section draws the strands of discussion together and concludes the paper.

II. India

Urban governance in India, despite the many national and sub-national programmes of the Indian state, is a relatively neglected subject both in policy making and in academia (Ahluwalia 2019). India being a democracy, the preponderance of votes being in the rural areas shifts the balance of political discourse to the rural sector.

This fundamental fact apart, there have been many national policies towards the development of urban areas in India. Presently, the national policy for urban governance in India is provided by the 74th Constitutional Amendment. According to the Twelfth Schedule of the Constitution, i.e., Article 243W, 18 aspects of governance are to be devolved to ULBs (Jha and Mathur 1996). Therefore, the macro-policy towards district urban planning and governance is clear.

The Constitution is also clear on the devolution of powers and functions based on which powers are to be devolved to urban local governments. However, while the Constitution is promulgated by the central government and legislature, it is State governments in India that are to devolve powers to ULBs. In this, as far as this article is concerned, both the States compared here (Karnataka and Telangana) fare equally poorly.

Though the constitution provides a national policy, the situation in Karnataka appears to be different. Karnataka has a document called 'Urban Development Policy for Karnataka', (GOK 2009), which deals with all aspects of urban development in the state. Taking only two aspects from its recommendations, I observe that the policy document makes a strong case for 'democratic local governance' and 'integrating spatial planning with economic development planning'. The document also suggests repealing certain Acts, and recommends giving more powers to local legislators. It is clear from the report that the state of 'democratic urban local governance' has not yet been fully implemented in Karnataka.

However, it is to the credit of the State of Karnataka that there is at least a draft policy document. Whichever government is in power can modify the document and implement it after such changes. Not many states in India have such draft urban policy documents. Since the draft policy document has not been implemented, we cannot make any comments on the same.

For the sake of examination, I take from Karnataka two districts: Dharwad and Udupi. From the State of Telangana, I take the case of the district city of Mahbubnagar. There is sufficient qualitative diversity in our sample. Dharwad is a city with a rich cultural and literary heritage. Udupi is a coastal, Hindu-dominated temple-city; Mahbubnagar is a city where around 40%of the population are Muslims.

The state of urban governance in the two cases of Dharwad and Udupi reflect partially the observations of the policy document (GOK 2009) mentioned above. But governance is not just about policy documents, it is about people -- citizens and the dwellers of these cities. Accordingly, I have relied on interviews with key persons in these three cities, including political figures, local bureaucracy, academics, journalists, and prominent citizens and observers of these cities.

Though the macro-policy of urban governance is to be guided by the 74th Constitutional Amendment, implementation of the policy is highly neglected. This is particularly so at district-level cities. Here, bureaucracy determines all the decisions. In Karnataka, it is the District Collector (DC) office that determines all governance (Vaddiraju 2013; Vaddiraju 2019). In Telangana, it is the Municipal administration that determines the decisions (Vaddiraju 2019). The attention paid to city governance is minimal because the responsibilities on these officials are far too many. For instance, the Ahluwalia Committee (2011) noted the following regarding ULBs in India:

> 'Urban local governments in India are among the weakest in the world both in terms of capacity to raise resources and financial autonomy. While transfers from state governments and the Government of India have increased in recent years, the tax bases of ULBs are narrow and inflexible and lack buoyancy, and they have also not been able to levy rational user charges for the services they deliver (pp. XXVI)'

Local government bodies are often weak and powers devolved to them and the resources they have are also limited (Swain 2013). This is at a time when economic growth is rapid and the private sector is expanding into these cities at a rapid pace (Shaw 2013). There is hardly sufficient local governance at district-level cities to be commensurate with the economic growth.

As a result, the cities are becoming chaotic. Basic civic services such as sanitation, drinking water, and solid waste management are often neglected. I have examined these aspects in Dharwad, Udupi, and Mahbubnagar in detail in previous work (Vaddiraju 2019). The questions I asked in that research were a) how is city planning taking place; b) how is the delivery of basic services such as drinking water and sanitation done; c) to what extent is the governance of the city effective; and d) are there any issues of social capital?

District-level towns are often neglected in terms of governance, and this is reflected throughout the country. The main reason for this is the policy bias of the successive governments towards mega-urban centres and agglomerations. The entire attention in urban governance so far has largely been towards the mega-cities (Gill 2013). The Ahluwalia committee (2011) notes the following regarding the smaller cities and towns in India:

> 'Smaller cities and towns should be treated differently from larger cities and metros – for funding, capacity building and reform content and timelines
> ◦ Funds for smaller ULBs should be channelled through intermediary institutions, and they should be encouraged to go in for pooled financing

> ◦ For Municipal Corporations and Municipalities, in addition to a regular window, a special window should be created specifically for projects that could be financed and executed via PPP route, or by leveraging private sources of funding(pp XXVIII).'

And the committee further notes:

> The Government of India will have to take a leadership role in financing a major part of the programme and, at the same time, facilitate and encourage the involvement of state governments and ULBs. State governments will have to contribute by way of a constitutionally mandated revenue-sharing arrangement with the ULBs. On their part, the ULBs will carry out reforms in governance and financing to deliver public services of specified norms to all including the poor. This should be done within a framework of accountability. Rising aspirations of the increasing numbers of people in urban India will make further demands on ULBs, and community participation will be an important factor in ensuring accountability. (ppXXVI).

Often the metropolitan and district planning committees are not constituted, and if constituted their functioning is minimal vis-à-vis urban governance. In such circumstances, the governance of ULBs shifts from constitutionally-elected functionaries to State government and its bureaucracy, as many of the functions and responsibilities are controlled by the State government and its line departments.

Besides the above, this article also argues that there are questions of social capital in governance in these district-level cities. By social capital, I mean the cooperation among political parties and among citizens, and the same reflecting in inter-ethnic relations. Social capital is important for these cities owing to inter-ethnic relations between religious communities, and secondly. in terms of the civil society and citizen group-oriented pressure on the city governance to deliver. I argue that while the question of inter-ethnic relations is a more complex issue, the same question of social capital is also relevant in making the cities deliver essential minimum services, such as drinking water, sanitation, and solid waste management.

To summarise, urban governance in India is supposed to take place according to the 74th Amendment to the Constitution. This Amendment stipulates elected urban local governments, at all levels of cities in general and at district levels in particular. In practice, however, State governments dilute the law at all levels. Although periodic elections take place, bureaucracy still calls all the shots in urban governance rather than the elected representatives.

To examine the implementation of the law, I have taken two States: Karnataka and Telangana. I have examined the implementation of the law at the district level in both States. I have discovered that instead of elected representatives, Deputy Commissioners take all the decisions regarding district-level urban governance in Karnataka. And instead of elected representatives, Municipal Commissioners take all the decisions in Telangana. To illustrate this argument, I have examined urban governance in Udupi and Dharwad districts of Karnataka and Mahbubnagar district in Telangana.

In addition to the above, I have also examined social capital — in making local urban governments work — in these cities. I have found social capital , at the time of the research, to be better in Udupi rather than Dharwad in Karnataka. And social capital is near absent in Mahbubnagar. I have also observed that urban civil society organisations are near absent in Dharwad, whereas they are active in Udupi. In the case of Mahbubnagar of Telangana, I have found that urban civil society organisations are near absent. And I have also noticed that Dharwad in Karnataka, with all its cultural heritage, and Mahbubnagar in Telangana, with all its religious syncretism, are also plagued with inter-ethnic tensions between different religious communities, reflecting the absence of social capital. Surprisingly, the city of Udupi has also, of late, developed similar tensions.

III. China

Much like in any other country, urbanisation in China is entwined with its broader history. Recently, Sun and Lisaia (2018) have periodised the history of urbanisation in China into three phases: the first phase from 1911 to 1949 i.e., during the pre-revolutionary China; the second phase from 1949 to 1978, wherein the influence of the Soviet Union and later processes of 'Great Leap Forward' and 'Cultural Revolution' have had their impact; and the third phase from 1978 till 2014. The period after 2014 is termed by the authors 'National New Type Urbanisation'.

According to these authors, these are historical transformations of China that have been synonymous with the modernisation of the Chinese state. To put it in their words: '*Between 1840 and 2017, China underwent three historical transformations in the quest to modernize the state*'. And,

> 'The first transformation saw the fragmented development of cities, mainly those that received foreign concessions. This became a significant step towards gaining national independence and re-organizing the structure of the state, but many problems remained'.

Sun and Lisaia point out that the second historical transformation began after the Chinese revolution in 1949 and had a decisive impact on the history of urbanisation:

> 'The impact of the second historical transformation on the development of Chinese cities, therefore, began with the first decade of New China which witnessed a powerful industrial base being laid with the support of USSR and the reconstruction of Chinese cities. Together with Soviet specialists, eight master plans for industrial cities were developed, based on Soviet urban planning theory, and a master plan for Beijing, the socialist capital of PRC [People's Republic of China], was proposed. In the late 1950s, under the influence of government campaigns such as the "Great Leap Forward", "Cultural Revolution" and the "Third Front Movement" urbanisation ceased. For the first 30 years of the PRC's existence, urbanisation was regarded as a phenomenon typical of capitalist countries and therefore received little attention from the government and scholars in this phase

The third historical transformation, beginning with reforms towards 'socialist market society', was equally decisive for urbanisation in China:

> 'In 1978 with the rise of Deng Xiaoping, the implementation of economic reform - 'the reform and opening-up' or 'internal reforms and external openness' policy - was initiated. The country altered its political course towards building 'socialism with Chinese characteristics', moving from class struggle to economic development. The foundation of reform was the principle of 'four modernisations' — defence industry, agriculture, science and industrial production.
>
> 'The most important changes in China's economy were ushered in with Deng Xiaoping's decision to establish five export zones — Special Economic Zones (SEZs) - located in favourable coastal areas near the Taiwan island, Hong Kong and Macau. These led to the rise of the cities of Shenzen, Zhuhai Shantou, Xiamen and Hainan. Foreign direct investment opened up new opportunities for the development of coastal cities. These zones had a concentration of enterprises focusing on products for export. The creation of SEZs became one of the key factors affecting the economic recovery of China."

Sun and Lisaia's article presents a highly-official version of Chinese urbanisation. For example, regarding migration they observe:

> 'At present, the country's largest economic centres attract millions of migrant workers every year who move from rural areas to work and live in the cities. China's internal migration has become the world's largest demographic shift: between 1978 and 2017, more than 500 million people became urban dwellers'

The above-discussed work by Sun and Lisaia is helps put an official historical perspective on urbanisation in China. It is interesting to observe, however, that these authors do not discuss the *hukou* system at any length.

However, the economic reforms of 1978 is supposed to have resulted in 25 million private enterprises in China, with urban employment accounting for 80% by 2017 (Wu, Yan, and Jiang 2018). This change has diluted the earlier political culture of organising society through work committees. And the socialist state's unity of society and state is supposed to be disintegrating since the 1980s. However, what replaced the party-state-society relationship in China? In attempting to answer this problem Wu, Yan, and Jiang ask two questions regarding the governance structures in urban China. These two questions go into the very heart of the transformations taking place in urban governance in contemporary China.

The first question that they ask is: 'why did Chinese local governments introduce new governance actors in communities?' They say that "*the history of community reforms in recent years in mainland China is marked by efforts to rebuild local integrating networks to ease the burden of the state by* *decentralising its power and delegating responsibility to other institutions*" (Wu, Yan, and Jiang 2018).

The second question that they ask is, 'how did the logic of government behaviour lead to different models of community governance?' To answer these questions, they take -- similar to the approach I have taken above regarding India -- a comparative view of two states and one district from each state. Their qualitative study covers two major provinces of China — Wuhan and Guangzhou; from Wuhan, they take Jianghan district to study, while from Guangzhou they take Yuexiu district.

In Wuhan, the state followed its own older pattern of strengthening the government to meet the growing needs of the people. The state did not carry out major governance reforms towards including the non-state actors in governance. This involved expanding its personnel and organizational strength for service delivery. The authors say:

> 'The ambition and dedication of the Jianghan District government were revealed in the strengthening of its institutions of power. The government and the party increased the number of government-employed community workers and improved the leading position of the party in the community, which demonstrated a kind of government-centric reform. (Wu, Yan, and Jiang 2018)

Whereas, 'in contrast, the professional SWOs (Social Worker Organisations) outside the traditional governance structure were introduced as new governance actors in Yuexiu District' of Guangzhou. And they go on to say that " *The former was [using] more governmental means and is, therefore, more conservative. The latter uses more social forces and is therefore more liberal.*"

However, after discussing the entire changes and experiments in local urban governance in detail, they hold the following: 'The situation is similar in both the districts. Although the traditional governance actors changed slightly in the reforms, the newly-designated actors' function and governance space are limited because of the limited autonomy of the CRCs [Community Resource Centres —the organisations created apart from the party to address the needs of local communities] in both the districts.

The reforms, though intended to create space for local community organisations, 'in Jianghan (i.e., in Wuhan) they mainly rely on administrative actors within the system. The delegation was accomplished through recombination and adjustment of the traditional governance structure.' On the other hand in Guangzhou. the 'Yuexiu District government established a parallel market system to replace the insufficient administrative system. I In terms of governance, some of the functions of the local governments were outsourced in Guangzhou to private market players, who in China were called Social Worker Organisations (SWOs). Whereas in Wuhan, the government relied on expanding its organisation and personnel owing to the growing urban needs. After elaborating this in detail, Wu, Yan, and Jiang (2018) observe:

> 'Although there is a slight difference between the reforms of Yuexiu, [i.e., wherein markets were brought in to serve governance] and Jianghan district [where the traditional party-government was strengthened and expanded to meet needs], there is no essential difference between the two areas in the

> leading force of the government. This finding verifies that there is no powerful civil society apart from the traditional government structure.'

They finally conclude by saying that the government, in reforming governance, is only looking for 'controllable helpers' and the reform is essentially 'temporary'. They conclude by saying:

> 'The so-called [governance] reform may be more of an amendment and supplement to existing governing measures. The impacts of the changes are therefore likely to be temporary.'

The above paragraphs clearly illustrate the ongoing experimentation in the field of urban governance in China. Wu, Yan, and Jiang greatly illuminate this process and hold a mirror to the fact that the party-state is alive and intact in urban governance in China. However, it must be noted that while these authors too have noted that China has 25 million private enterprises today, and the ratio of urban employment to the total employment is 80%, they still do not make clear to us whether the *hukou* system has been totally dismantled, or it is still existing.

IV. Discussion & Conclusion

The Indian case of three district-level cities from two States clearly shows that these cities suffer from severe neglect in terms of governance. This is particularly the case in Dharwad and Mahabubnagar; whereas, in Udupi, I find the situation somewhat better. And, also that this situation of governance deficit, is partly compensated when there is citizen action to make the government work at the city level.

I take Udupi city to be an example of better governance and better social capital between citizens as the reason for the same. However, of late fissures have appeared in the social capital of Udupi citizenry too. This Brahmin caste and Hindu religion-dominated city now faces challenges from the Dalit groups of the city and from outside. Not only that, recently there were Hindu-Muslim communal tensions too in Udupi. The fissures of Indian society are reflected here too.

These conflicts are a testimony to the complexity of Indian society. Also, I have argued that in the cities of Dharwad and Mahabubnagar, social capital appears to be lacking a) in terms of making government work, and b) in terms of inter-ethnic relations.

In the case of China, the governance reforms do not provide much basis to call the emerging SWOs in Guangzhou 'civil society'. As I noted earlier, what seems to be happening in Guangzhou is essentially outsourcing some of the social care functions to market actors. The latter can be called 'civil society' only with great caution. In the context of Chinese urban governance, applying the related concept of 'social capital' appears to be far-fetched.

What we have now in China, as is illustrated by Wu, Yan, and Jiang, is some room for manoeuvre for markets in governance, by way of outsourcing some of the functions of the state. This in no way reduces or dilutes the grip of the party-state over local society or government. As I mentioned in the beginning, the process of urbanisation in China indicates that there is a substantial amount of experimentation with different forms of local urban governance, the predominant being that of the state-dominated one. The Chinese state, even when involving SWOs, outsources only those functions that either it cannot perform or does not want to. From the above discussion of urban governance in India and China, I propose the following description:

Table-1: Urban Governance in India and China: A Comparative View

Country/Aspect	Urban local self-governments	Markets, independently/ in partnership with governments	Civil Society and Urban civic action Independently/ Partnership with government
India	**Weak**	**Strong**	**Weak**
China	**Strong**	**Weak**	**Weak**

Comparisons between China and India, in terms of whichever aspects, have to come to grips with the fact that both are two different political, economic and social systems. In terms of urbanisation, there are some similarities between the two. As some noted experts on Indian urbanisation write (Kundu:2014), "if Indian urbanisation is exclusionary, the Chinese counterpart is no less exclusionary." Similarly, civil society and social capital can be effective for governance in India and China. At the same time, we should keep in mind that civil society and social capital are contested and can be intrinsically contradictory tools.

Governments in both India and China have found civil society useful at times, and at other times problematic. Therefore, they have imposed curbs on civil society, social capital, and citizen action. In India for example, at the national level, the United Progressive Alliance (UPA) regime at the union has found civil society progressive and, to some extent, reliable support, whereas the current National Democratic Alliance (NDA) regime at the union is decidedly not in favour of civil society. Likewise — and this is with many caveats — the Chinese state too has found civil society and social capital as useful tools to promote government and 'governance' at some times, and a problem at other times.

I tend to believe that given the market orientation of both the polities in the recent past, and given the inter-city and intra-city inequalities, social capital can be a useful tool for the promotion of effective governance. If the polity is open, and not just the economy, it has more space for these organisations; and if the polity is closed, there will be less space for civil society. However, the same polity can sometimes provide more space to civil society than before. These vary from time to time with the same structure of the state being in place.

We can conclude that, as Table 1 illustrates, as far as urban governance is concerned, party-state is all that there is in China, all experiments notwithstanding. The party-state's relationship with markets and civil society in governance is rather instrumental and pragmatic. The party-state takes all the decisions of governance and markets and civil society dances to that tune.

The Indian case reflects that, though the laws for local representative governments exist, urban governance and urban civil society are still weak, compared to the strength and growth of urban markets. Indian cities are bursting at the seams with markets. Local government and 'governance' with equal, commensurate strength to regulate these markets, and rein in the markets, and an urbane civil society to stand up to the injustices of markets, at the same dealing with the challenges of multiple dimensions of urbanisation, and a state that can champion the rights of all urban communities successfully, are all still a far cry in India. And therefore, the challenges of urbanisation in both countries are only half-addressed as of now.

References

Ahluwalia, Isher Judge *et al* (2011) *Report on Indian Urban Infrastructure and Services*, New Delhi: Government of India.

Ahluwalia, Isher Judge (2019) 'Urban Governance in India' in *Journal of Urban Affairs,* Vol.41, No.1, pp83-102.

da Cruz, Nuno F, Philipp Rode& Michael McQuarrie (2018) 'New Urban Governance: A Review of Current Themes and Future Priorities' in *Journal of Urban Affairs*, Vol. 41 No.1 pp1-19.

Feng, Cai and Meiyan Wang (2010) 'Urbanisation with Chinese Characteristics' in Garnaut, Ross, Jane Golley and Ligang Song (Eds) *China: The Next Twenty Years of Reform and Development*, Sydney: ANU Press, (accessed from JSTOR).

Gill, Rajesh (2013) 'The Academic Bias against Towns: A Cultural Audit', R.N. Sharma and R.S. Sandhu (Eds) *Small Cities and Towns in Global Era: Emerging Changes and Perspectives*, Jaipur: Rawat Publications, pp 84-98.

Government of Karnataka (2009) *Urban Development Policy for Karnataka* (2009) Bangalore: Government of Karnataka.

Hashim, S.R (2020) 'Inclusive Urbanisation' Key Note Paper, presented at the 20th Annual Conference of the Indian Association of Social Science Institutions, at the Institute for Social and Economic Change, Bengaluru, on 27th February, 2020.(mimeo, ISEC).

Howell, Jude (2011) 'Civil Society in China' in Edwards, Michael (Ed) *The Oxford Handbook of Civil Society*, Oxford and New York: OUP, pp.159-171.

Jha,S.N. and P.C.Mathur (1999) *Decentralization and Local Politics*, New Delhi: Sage.

Kundu, Amitabh (2014) 'India's Sluggish Urbanisation and its Exclusionary Development' in Mc Granahan, Gordon and George Martine (Eds) *Urban Growth in Emerging Economies: Lessons from BRICS*, London and New York: Routledge, pp191-232.

Mathur, Kuldeep (2008) *From Government to Governance: A Brief Survey of the Indian Experience*, New Delhi: National Book Trust.

Mc Granahan, Gordon *et al* (2014) 'China's Radical Urbanisation and Bringing Capital and Labour Together Step by Step' in Mc Granahan, Gordon and George Martine (Eds) *Urban*

Growth in Emerging Economies: Lessons from BRICS, London and New York: Routledge, pp 55-98.

Metzger, Thomas A (2001) 'The Western Concept of Civil Society in the Context of Chinese History' in Sudipta Kaviraj and Sunil Khilnani (Eds) *Civil Society: History and Possibilities*, Cambridge: Cambridge University Press, pp. 204-232.

Shaw, Annapurna (2013) 'Emerging Perspectives on Small Cities and Towns' in R.N. Sharma and R.S. Sandhu (Eds) *Small Cities and Towns in Global Era: Emerging Changes and Perspectives*, Jaipur: Rawat Publications, pp36-54.

Sullivan, Helen (2009) 'Social Capital' in Davies and Imbroscio (eds) *Theories of Urban Politics*, Los Angeles, London and New Delhi: Sage, pp 221-238.

Sun, Yimin and Daria Lisaia (2018) 'History Matters: Chinese Urbanisation as an Emergent Space', *Urbanisation*, Vol.3. No.1, pp 1-16.

Swain, Biraj (2013) 'Small Towns, their Limited Resourcing Options and Equity Deficits' in R.N. Sharma and R.S. Sandhu (Eds) *Small Cities and Towns in Global Era: Emerging Changes and Perspectives*, Jaipur: Rawat Publications, pp 98-111.

Vaddiraju, Anil Kumar (2013) 'A Tale of Many Cities: Governance and Planning in Karnataka' *Economic & Political Weekly,* Vol. XLVIII, No.2 .pp 66-69.

Vaddiraju, Anil Kumar (2014) 'On Civil Society Again: Civil Society, State and Public Policy in South India', *Studies in Indian Politics*, Vol. 2. No.1, pp 55-66.

Vaddiraju, Anil Kumar (2019) 'District-Level Urban Governance Policies in India: Cities of Neglect?' *Urban India*, Vol.39, No.1 Jan-June, pp.134-142.

Vishal, R, Shalini Singh and Kala S. Sridhar(2021) 'Municipal Finances and Decentralized Government : Lessons from India and China' in Kala S. Sridhar and Li Jingfeng (Eds) *The Rise of India and China*, Oxon and New York: Routledge, pp 231-54.

Woolcock, Michael (2011) 'Civil Society and Social Capital' in Edwards, Michael (Ed) *The Oxford Handbook of Civil Society*, Oxford and New York: OUP, pp.197-208.

Wu, Xiaolin, Huiqi Yan and Yongxi Jiang (2018) 'How are New Community Structures Formed in Urban China? A Case Study of Two Cities, Wuhan and Guangzhou', *Asian Survey*, Vol. 58. No. 5. pp 942-965.

Notes

[#] Acknowledgements: Immense thanks to the anonymous referee for enormously helpful comments. I am also immensely thankful to Professor Kala Seetharam Sridhar for providing some documents cited in the paper, and for Professor Sunil Nautiyal for reading the paper and providing comments. Help is gratefully acknowledged

[1] Kundu(2014) discusses both the positions and argues his case for sluggish growth of urbanisation in India. He also demonstrates how the nature of Indian urbanisation is 'top heavy' and how smaller district and lower tier cities are neglected in growth and governance. He also discusses how increasingly the urbanisation process in India is market driven.

Indian Public Policy Review 2022, 3(2): 58-77

Inadequate Parliamentary control over Public Revenue

Legislative silence or failure of CAG?

T Selvaraju*

Abstract

The purpose of this paper is to study the level of parliamentary control over public finance in India for ensuring accountability and transparency expected in a democratic form of governance. As per the Constitution of India, neither any money shall be collected nor the collected money be spent without the approval of the Parliament or the State Legislature, as the case may be. The accountability and transparency expected in spending should equally apply to revenue collection also, as they are the two sides of public finance. While the parliamentary control over public spending is complete with the system of parliamentary approval for spending and monitoring of the spending against its approval, through Appropriation Accounts, such control is not complete in respect of public revenue, as there is no parliamentary procedure to monitor the realisation of all revenues authorised by it. Consequently, crores of rupees of public revenue authorised by Parliament/Legislature could remain uncollected without its knowledge. Introduction of a Receipts Accounts showing the details of unrealised revenues with reasons and its presentation to Parliament/Legislature would fill the gap in parliamentary control and transparency in realisation of public revenue

Keywords: Parliamentary control, Management of Public Finance, Unrealized Public Revenue, Appropriation Accounts, Receipts Accounts

Publication Date: 18 March 2022

* T Selvaraju is a retired Senior Deputy Accountant General from IA&AS

I Statement of issue

1.1 Importance of management of public finance and parliamentary control

In a parliamentary democratic form of governance, supremacy of the collective body of people's representatives (Parliament), accountability of the government (having support of majority of representatives) to the Parliament during tenure of government and transparency in governance for public scrutiny of government's actions are the basic canons.

Though accountability and transparency are applicable to all activities of governance, the same in handling of public finance shall be the most mandatory as nearly everything, from a nation's survival to its growth, depends on its economic worth. Further, considering the susceptibility of public money in the hands of power, a complete parliamentary control and transparency in management of public finance is imperative.

The system in place for control of public finance in India should provide an assurance to the people that the Parliament/State Legislature is ensuring accountability of executive government and transparency in financial management, both in revenue mobilisation and their spending.

The system in place for control of public finance in India should provide an assurance to the people that the Parliament/State Legislature is ensuring accountability of executive government and transparency in financial management, both in revenue mobilisation and their spending.

1.2 Objectives of the Study

The objectives of this study are to (i) assess the present level of parliamentary control over public finance - both revenue and expenditure, (ii) examine the need for bridging gaps in parliamentary control and (iii) evolve a system for adequate parliamentary control over management of public finance.

1.3 Methodology and coverage

The system and procedure followed for management of public finance by Union and State/Union Territory governments having Legislature are generally the same. As such, the Study covers both Union Government and State/UT Governments with Legislature. The terms Parliament, parliamentary control and government referred to in this Study Report hereinafter appropriately include State/UT Legislature, State/UT Legislature's control and State/UT (having legislature) governments respectively.

II Existing level of Parliamentary control over Public Finance

2.1 Parts of public money

Public money is kept in three parts viz. Consolidated Fund, Contingency Fund and Public Account (Articles 266, 267, 283 and 284 of the Constitution of India). The Consolidated Fund of India or States is the part where all government's own receipts are kept and spent. The Parliament/State Legislature has full control over this fund.

The other two parts viz., the Contingency Fund (a form of imprest placed at the disposal of government to meet unforeseen expenditures for which parliamentary approval was not obtained earlier) and the Public Account (keeping/accounting of other public moneys like Small Savings, Court deposits, Reserve funds, etc.) are incidental. The Government's role in the case of Public Account is only that of a custodian/banker.

2.2 Classification for allocation and accounting of public money

A six-tier classification structure with 15 digits code (commonly known as Head of account) viz., Major Heads (4 digits), sub-major heads (2 digits), Minor heads (3 digits), sub-heads (2 digits), Detailed heads (2 digits) and object heads (2 digits – not operated for Receipts Heads) is adopted for allocation of funds for expenditure by Parliament for various purposes and their spending and accounting. Similarly, the receipts are also accounted as per the classification code.

2.3 Stages in management of public finance

As per the Constitution, no tax shall be levied and collected except by authority of law (Article 265) and no amount can be drawn from the Consolidated Fund without parliamentary approval (Article 266 (3)).

Management of public finance involves three stages viz., (a) parliamentary approval for collection of revenue and their spending, (b) actual collection of revenue and spending by the executive government and (c) accounting the collection and expenditure and their submission to Parliament/State Legislature.

2.3.1 Parliamentary approvals for mobilisation of revenue and spending

As envisaged in the Constitution (Art.112/202), Governments present an Annual Financial Statement (Budget) showing estimated receipts and expenditure of the government to Parliament/Legislature for approval.

The Budget documents comprise, *inter alia*, Expenditure Budget giving details of estimated expenditures (expenditure to be charged upon the Consolidated Fund and other expenditure to be voted (authorised) by the Parliament/the State Legislature) under various heads and Receipts Budget with details of estimates of tax/non-tax/capital receipts along with explanation for the estimation.

The budget documents also include various statements like (a) statement of tax revenues raised but not realised in respect of some principal taxes and statement on arrears of non-tax revenues, as mandated by the Fiscal Responsibility and Budget Management Act, 2003, (b) statement of revenue foregone, (c) statements of liabilities, guarantees given by the government, statement of assets, etc.

2.3.1.1 Approval for expenditure

Expenditures proposed in the budget

The parliamentary approval for expenditure proposed in the Budget involves two stages, presentation of "Demands for Grants" and passing of the Appropriation bill.

The proposals for getting the approval estimated expenditure (the portion of estimates related to charged expenditure shall not be put to vote of the Parliament) from the Consolidated Fund are presented (Art. 113/203) in the form of 'Demands for Grants' (one main Demand for grants comprising all the ministries/departments and Detailed Demand for Grant for each ministry/department).

After passing of Demands for Grants, Parliamentary approval for withdrawal of the amount from the Consolidated Fund is sought through the Appropriation bill (Article 114/204). This Appropriation Bill indicates the fund provisions for various expenditure (voted grants and the charged appropriations) as per the classification code. This bill would become an Appropriation Act with assent of the President/Governor.

For incidental and other expenditures

Apart from the budgetary procedure, the Constitution also envisages other procedures for incurring expenditure from Consolidated Fund. They are (i) Supplementary grant or appropriation' (Art.115 (a)/205 (a)) to enhance budget provision subsequently, (ii) Vote on account (Art.116 (a)/206 (a)) to meet expenditure till approval of Budget for the year, (iii) Vote of credit (Art.116 (b)/206 (b)) for meeting unexpected expenditures, the details of which cannot be given in the budget on account of magnitude or indefinite character of the service, (iv) Exceptional grant (Art.116 (c)/206 (c)) for expenditure not forming part of current service of any financial year and (v) Demands for excess grants (Art.115 (b)/205 (b)) for regularisation of excess expenditure incurred by the government during a financial year over and above the grants authorised by Parliament/State Legislature and the charged expenditure shown in the Appropriation Act for that year.

2.3.1.2 Approval for mobilisation of resources

The taxation proposals of the government for the ensuing year are introduced as Finance bill (Articles 265 and 110 (1)(a)/199 (1)(a)), immediately after presentation of budget. It contains the details of imposition of new taxes and abolition, remission, alteration or regulation of existing taxes. It is accompanied by a memorandum explaining the provisions of the bill and their effect on the finances of the country. The Finance bill is normally considered and passed by the Lok Sabha/Legislative Assembly after the 'demands for grants' have been voted i.e. after the total expenditure authorised by it is known. With the assent of the President/Governor, this bill becomes the Finance Act.

2.3.2 Collection and spending of money by the executive government

A treasury system, with Pay and Accounts Offices (PAOs)/Treasuries, is in place for transaction of public money and their accounting. The governments have an arrangement with the Reserve Bank of India for banking facilities.

The departmental officers, entrusted with the responsibility of collection of government revenue, are to collect the revenues and remit them into treasury/banks (through a challan indicating the head of account) for the credit of the government accounts concerned. Individuals/other entities can also directly remit dues to government accounts.

Similarly, officers for incurring expenditure (generally known as Drawing and Disbursing Officer, DDO), are to submit bills to the treasury/PAO seeking the amount required for spending mentioning the appropriate head of account. On passing (i.e. after disbursing the amount), these bills would be termed as vouchers.

2.3.3 Accounting and presentation of accounts to the Parliament

The accounts of governments are maintained on cash basis[1]. From the challans and vouchers, initial accounts like treasury accounts, monthly accounts of the government are compiled. Based on these, the Annual Accounts viz., Finance Accounts and Appropriation Accounts are compiled/prepared by the Controller General of India/Ministries/Comptroller and Auditor General of India/State government of Goa/UT of Puducherry, as the case may be. These accounts, after scrutiny and certification by the Comptroller and Auditor General of India, are presented to the Parliament/State Legislature.

The **Finance Accounts** is an account of both actual receipts and expenditure/disbursements under all three parts of government accounts, along with government assets (investments) and liabilities (borrowings).

The **Appropriation Accounts** is an account of the expenditure incurred by the government against the funds approved by Parliament/Legislature for various purposes from the Consolidated Fund. This Account depicts head-wise details of funds approved for the year and the actual expenditure against them with resultant savings (unspent approved funds) or excess (expenditure over and above the approved funds). The reasons/explanations of the government for significant saving or excess are incorporated therein.

2.4 Auditing and placing of Audit Reports in the Parliament/State Legislature

The Comptroller and Auditor General of India (CAG) also audits, *inter alia*, the receipts and expenditure of the governments and submits his Audit Reports thereon to the President/Governor for their placement in Parliament/State Legislature (Articles 149 and 151 and Sections 13 and 16 of CAG's (DPC), Act 1971).

2.5 Parliamentary monitoring through the Accounts and Audit Reports

Of the two Annual Accounts, Finance Accounts is not examined in detail as it depicts only the actual receipts and expenditure/disbursements. All the Audit Reports and Appropriation Accounts are examined in detail by a Parliamentary/Legislature Committee viz., Public Accounts Committee (PAC). After obtaining further explanation from the government, PAC makes appropriate recommendations for further action by the government. The Reports of PAC containing its recommendations for further action and its Reports on Action Taken by the government on those recommendations are presented to the Parliament/State Legislature.

PAC examines Appropriation Accounts to see, *inter alia*, whether the entire approved funds have been spent for the purpose for which they were approved. It further investigates the reasons for spending more or less than the monies approved. All excess expenditures brought out in Appropriation Accounts are to be regularised by Parliament/Legislature through 'demands for excess grant'.

2.6 Inadequacy of provision for control over revenue realisation

From the above, it is evident that, in the case of expenditure, the control starts with authorisation of expenditure (Appropriation Act specifying quantum of funds approved for each item of expenditure) by the Parliament/Legislature. The compliance of the government is watched through Appropriation Accounts submitted to it. PAC examines the Appropriation Accounts in detail for fixing accountability for not spending the approved provision of funds or incurring excess expenditure. All excess expenditures are to be regularised by the Parliament/State Legislature. In addition, CAG's Audit Reports on expenditure are also available for further accountability on other financial improprieties.

In respect of revenue also, the control starts with authorisation for mobilisation of resources (Finance Act); but there is no mechanism to watch whether the government has collected all the revenues authorised by Parliament/State Legislature or not, besides the Audit Reports on receipts.

Thus, accountability of the executive government and transparency in respect of expenditure is ensured through two tools, Appropriation Accounts and Audit Reports on expenditure. But in the case of revenues, only one tool, the Audit Reports on Receipts is available to the Parliament/Legislature.

The existing Constitutional and other statutory provisions for the parliamentary control and the gap in monitoring of revenue collection is illustrated in the table below:

Nature of control	Revenue	Expenditure
Initial parliamentary approval (for revenue collection and incurring expenditure)	Budget (Article 112 for Union/202 for States)	
	Article 265 – No tax be levied without authority of law	Article 266 (3) – No money be drawn except in accordance with law
	Article 110(1)(a) - Finance Act (Non-tax revenues are also levied by government as per power delegated by various Acts)	Articles 114, 115,116/ 204, 205, 206 - Appropriation Acts
Actual Receipts and expenditure (Transparency)	Finance Accounts (Section 11 of CAG's (DPC) Act)	
Monitoring compliances of Parliament's approval (Accountability and Transparency)	?	Appropriation Accounts (Section 11 of CAG's (DPC) Act)
Accountability for financial impropriety (Accountability and Transparency	Audit Reports (Section 13 of CAG's (DPC) Act)	Audit Reports (Section 16 of CAG's (DPC) Act)

Thus, in the existing control mechanism, while even a rupee cannot be spent from the Consolidated Fund without the knowledge of Parliament/Legislature, crores of rupees of revenue to be collected as authorised by it could remain uncollected without its knowledge.

When the fiscal management and monetary results (fiscal/revenue surplus or deficit) depend on both revenue collection and expenditure incurred, the efficiency, transparency and accountability expected of in spending should equally be applicable to revenue realisation also. But Parliamentary control over revenue realisation is not as complete as that of expenditure. Consequently, a monitoring system to watch the collection of unrealised revenue to its finality is absent. Thus, a significant gap is in parliamentary control over revenue realisation.

III Causes for the gap in control over public revenue

3.1 Is it due to Legislative silence?

The importance of management of public finance was appropriately felt by the Constituent Assembly, as may be noted from the speeches given below:

(i) Dr Ambedkar: "...He (CAG) is the one man who is going to see that the expenses voted by the Parliament are not exceeded or varied from what has been laid down by Parliament in what is called the Appropriation Act...". (Constituent Assembly Debates, Volume VIII, May 30, 1949)

(ii) Shri T. T Krishnamachari: "... I agree that what we want is that the total amount of financial resources available both for the Centre and the units has to be augmented and it has to be augmented if the ultimate purpose of this Constitution, namely the economic betterment of the common man is to be undertaken. ..." (Constituent Assembly Debates, Volume XI, November 25, 1949).

(iii) Dr B Pattabhi Sitaramayya: '... no matter how perfect the Constitutions may be, no matter how numerous may be checks and balances and safeguards for the right conduct of business of the future, it is money that counts, and we have to deal with about 370 crores at the Centre and as much money in the Provinces, and if all this money is not spent aright, and if the people deliver cheap gibes at men like me who count rupees, annas and pies, and to who, every rupee means 16 annas and every anna means 12 pies, then there is no government at all worth mentioning, it is anarchy, it is chaos. It is loot. It is dacoity. And who is to control this? Is it to be man who is appointed by the Ministry that should control this? No. The Comptroller and Auditor General must be as supreme and independent as the Judges of the Supreme Court ...'. (Constituent Assembly Debates, Volume XI, November 25).

(iv) The President of the Constituent Assembly, in his concluding remarks on 26th November, 1949 (volume XI): '... Another independent authority is the CAG who will watch our finances and see to it that no part of the revenues of India or of any of the States is used for purposes and on items without due authority and whose duty it will be otherwise to keep out accounts in order, when we consider that our governments will have to deal with hundreds of crores, it becomes clear how important and vital this department will be.' (Constituent Assembly Debates, Volume XI, November 26, 1949).

Accordingly, they have incorporated constitutional provisions for maintenance of accounts (Article 150) and audit of accounts (Article 151) by an independent authority, CAG of India and submission of Accounts and Audit Reports to Parliament/Legislature (Article 152). However, regarding CAG's duties, they allowed *status quo* (Article 149), i.e., CAG was to continue to perform the same duties he/she was discharging immediately before commencement of the Constitution, until provision in this regard is made by the Parliament.

In the Parliament Act subsequently enacted in 1971 detailing the duties and powers of CAG - Comptroller and Auditor General's (Duties, Powers and Condition of Service) Act, 1971) -, there is explicit mention only for preparation of Annual Accounts showing receipts and disbursements and Appropriation Accounts[2] , in addition to provisions for audit of expenditure and revenue (Section 13 and 16 respectively).

As per section 16, CAG shall audit all receipts which are payable into Consolidated Fund of India/States/UTs having Legislative Assembly and satisfy himself that the rules and procedures on that behalf are designed to secure an effective check on the assessment, collection and proper allocation of revenue and being duly observed and shall make for this purpose such examination of the accounts as he thinks fit and report thereon.

When section 16 mandates the CAG to audit all receipts payable and to make examination of the accounts, a specific mention could have been made appropriately for a Receipts accounts showing the uncollected revenues, as the Finance Accounts showing only actual receipts and disbursement would not provide adequate input for audit of all receipts payable.

Thus, there is no explicit provision in the Constitution or in the Statute for preparation of an Accounts showing the uncollected revenue dues to monitor their realisation.

3.2 Is it due to the failure of CAG?

Though Section 16 specifically requires CAG to examine the accounts to satisfy himself that the rules and procedures are designed to secure an effective check on the assessment, collection are being duly observed, no accounts indicating that all the receipts payable into Consolidated Fund have been prescribed by CAG. Curiously, even CAG's Revenue Audit Manual on Direct Taxes, 2015 providing guidelines for audit of direct taxes, while referring to his authority to audit the receipts, in paragraph 1.2 omitted the word 'examination of the accounts' mentioned in Section 16. The portion is reproduced below:

'... Section 16 of the C&AG's DPC Act authorises C&AG to audit all receipts (both revenue and capital) of the Government of India and of Governments of each State and of each Union Territory having a legislative assembly and to satisfy himself that the rules and procedures are designed to secure an effective check on the assessment, collection and proper allocation of revenue and are being duly observed.' (Revenue Audit Manual, 2015, 1)

The Manual, while further listing out the main items of work to be undertaken during Compliance Audit (*ibid* paragraph 4.4.3, 17) and the records and statistical information required to be called for conducting audit (paragraph 6.2 (c) and Appendix 11, *ibid*), mentioned only 'Getting Demand and Collection (DCR) Register' and "Hard and soft copies of Demand & Collection Register (D&CR) in respect of assessed cases" and Collection of Tax in Arrears in the case of audit of Tax Recovery Offices.

Thus, it is evident that no accounts enabling audit of all receipts payable into Consolidated Fund have been prescribed. The limitations of receipt audit relying on only the Demand & Collection Register and Data on collection of tax in arrears as furnished by a Revenue collecting Department are detailed in Paragraph 4.3 below.

As per Article 150, the accounts of the Union and of the States shall be kept in such a form as the President may, on the advice of CAG, prescribe. Accordingly, CAG could have prescribed a form of accounts for monitoring unrealized Receipts and prepared a Receipts Accounts based on that and presented to the Parliament/Legislature.

IV Need for parliamentary monitoring of revenue realisation

4.1 Finance Accounts – not enough for monitoring of Revenue collection

Finance Accounts, as already discussed, gives only the details of actual receipts and disbursements. Accordingly, the contents of the Finance Accounts would not be sufficient to monitor what the Parliament/Legislature intended and what the executive government has done. Consequently, an additional arrangement has been made for the purpose for Expenditure (Appropriation Accounts), besides the Audit Reports on expenditure. But there is no similar arrangement in respect of Revenue collection, besides Audit Reports.

The grounds/justification for preparation and submission of Appropriation Accounts to the Parliament are equally applicable to the revenue, as the collection of which was also authorised by it. The authorising body should know whether the entire revenue authorised/intended by it is collected or not and if not, the reasons therefor.

4.2 Limitations of Statements on 'Revenue not realised'

The Fiscal Responsibility and Budget Management Act (FRBM Act) in 2003 and the Rules, 2004 made thereunder, in order to ensure greater transparency in fiscal operation in the public interest, *inter alia*, compels the Central government to make more disclosures and one of such disclosures is made with Receipt Budget in two Statements (i) Tax Revenue (principal taxes) raised but not realised and (ii) Arrears of Non-tax revenue (Receipt Budget, Union government, Annexures 5 and 6).

The statement on tax revenue gives the age-wise pendency – from over one year to over 10 years – under two heads viz., amounts under dispute and amounts not under dispute. The statement on non-tax revenue gives age-wise pendency 0-1 year to over 5 years. This provides transparency to an extent, but without any system for fixing accountability for non-collection. Further, the disclosures are also not adequate, timely, and complete. The figures are not certified by any external agency and as such it would not satisfy even the aspect of transparency, as detailed below:

i. In case of Tax, it covers only principal taxes. The positions of other taxes are not given. In respect of non-tax revenue also, it is not clear whether all arrears are included.
ii. The two statements, each of a page only, gives only the consolidated position of unrealised revenue.

iii. The amounts shown as not realised are only against the demand raised. It does not give an assurance that demand has been raised in all cases.

iv. The two statements depict the position of non-realisation as of two years prior to the year in which it is presented. For instance, the Receipt Budget for 2021-22 gives position at the end of 2019-20.

v. The reasons for non-realisation tax except 'under dispute' are not given (the nature of the dispute is, also, not given).

vi. The two statements did not give any opening positions, amount collected/waived therefrom, etc. The correctness of the figures is not certified by any external/independent agency.

4.3 To make the Receipt Audit effective

In the existing cash-based accounting system, financial activities cannot be easily traced unless there is flow of cash. For instance, if a leaseholder of government property has been not paying the lease for years together, and the transaction did not find a place in the Finance Accounts, Audit may not easily come to know of this due. Under the circumstances, the Auditor has to rely mainly on the figures given by the departments.

An observation of CAG of India given below, is an indicator of the lacuna in this regard:

"We have compiled this Chapter based on data mainly obtained through the Central Board of Excise and Customs. It (CBEC) provided data for the 3-year period FY11, FY12 and FY13 relating to various performance parameters such as preliminary and detailed scrutiny, refunds, arrears in realization, pendency of call bookcases, etc., in August 2013. However, we observed that in some instances, data furnished did not tally with information furnished for the last Audit Report (AR No.17 of 2013) and would need reconciliation by the department. There is an urgent need to improve the quality of data and of monitoring aspects in respect of Service Tax. Authorities such as Directorate General of Service Tax, Mumbai, Directorate General of Inspection, Customs and Central Excise, New Delhi, Directorate General of Central Excise (Intelligence), New Delhi, etc., should ensure maintenance or reliable data for use, *inter alia*, by Audit. Review of the formats of Monthly Technical Report Annexures in Service Tax to ensure that important items such as conduct of detailed scrutiny are not lost of, is vital. There is no periodic return in the department which monitors the number of cases and amount of interest paid in respect of refunds. In the current scenario where there is no distinct accounting head for accounting interest on refunds, it is not clear how accurate and reliable the figures provided are..." (Comptroller and Auditor General of India 2014, 23-24)

Thus, an exclusive and additional Accounts showing the unrealised revenue is a prerequisite to fully serve the objective of receipt audit.

4.4 To make available details of unrealised revenue on regular basis

Parliament is entitled to know whether the monies as intended by it have been collected or not. They are also entitled to know the reasons for non-collections; if possible, the details of the institutions/bodies/organisations/individuals from which/whom significant portions remain to be collected. In the absence of the details on a regular basis, they can only be obtained either under Right to Information Act or by the Members of Parliament through questions. For instance, a parliamentary question answered in the Parliament by the Minister of State for Ministry of Finance is given below (26th August 2011):

Question: Will the Minister of Finance be pleased to state

a. Whether the government has constituted a task force for recovery of income tax arrears;
b. If so, the details thereof;
c. The amount recovered by this task force as on 31 December 2010; and
d. The time by when the government is likely to recover the full arrears?

Answer:

a. Yes sir
b. The Income Tax Department has constituted task force from time to time for recovery of income tax arrears and with an objective to evolve and implement a multi-pronged strategy for collection of arrear tax
c. The department does not maintain separate data about the recovery made by the task force. However, the amount of tax arrears recovered by the department during last two financial years and during financial year 2010-11 as on 31 December 2010 is as below:

Financial year	Amount collected (Rs in crore)
2008-09	10,016
2009-10	11,939
2010-11 as on 31.12.2010	7,079

d. The raising of demand and collection of outstanding taxes is a continuous process, and all out efforts are made by the Income Tax Department to collect the outstanding taxes. As tax arrears is not a static concept, it is not possible to recover arrears in full at any given point of time.

Thus, as of now, neither Parliament nor citizens knows the names of even major defaulters of government dues and details of action taken by the government, on a regular basis.

4.5. Transparency and Parliament's obligation to ensure revenue recovery

In the judgment (6 January, 2014) on the audit jurisdiction of CAG on the accounts of the license holder to establish, maintain and operate cellular mobile telephone services, the High Court of Delhi observed (para 16) that the three features of 'club governance' viz., (i) informality, (ii) reliance on knowledge acquired by insiders by virtue of their insider status and (iii) screening from public scrutiny and accountability had to be replaced or displaced by (i) standardisation and formality, (ii) the provision of systemic information accessible both to insiders and outsiders and (iii) strengthening the control mechanism and public reporting (2014).

The Supreme Court of India also observed, in its judgment (17 April 2014) on the appeal of the above case along with other civil appeal that Parliament has an obligation to ascertain whether the entire receipts by way of license fee, spectrum charges, have been realised by the Union of India and credited to the Consolidated Fund of India.

Thus, the highest court of the country also wishes a complete parliamentary monitoring of revenue realisation.

4.6. Significance of receipt realisation for fiscal management and economic growth

Good governance and better financial management cannot be confined to the quality of spending alone. The efficiency and effectiveness in spending the money collected should be ensured in collection of revenue also. The financial deficit depends both on receipts and expenditure. There may be other easier options to keep the fiscal and other deficits under control like restriction of expenditure at the cost of development. But more economic growth can be achieved, and welfare schemes implemented with the same level of fiscal deficit, provided all the revenue dues are collected.

The fiscal deficit[3] of the Union government, for the year 2019-20 was Rs 10,31,126 crore (Comptroller and Auditor General of India 2021, para 1.3). As per the Receipts Budget for 2021-22, the tax revenue (principal taxes) raised but not realised and arrears of non-tax revenue were Rs 12,97,975 crore and Rs 3,32,428.66 crore respectively, as at the end of reporting year 2019-20. The collection of these arrears alone would have been enough to set off the fiscal deficit of the year. In lieu of the realisation, the alternative course of option[4] to the governments would be borrowing/using the public account fund and thus the Union government created the above additional liability with inherent interest burden. The above position would highlight the importance of the realisation of receipts. A systemic parliamentary monitoring would have its positive impact on the level of revenue collection facilitating better finance management.

4.7. Applicability of concept of non-performing assets to public finance

Non-performing Asset, a classification of loan by the financial institutions, is an asset not yielding any income. The concept of non-performing assets could be equally applicable to public finance also. The unrealised revenue is only a non-performing asset as it is not available to the government for its use, resulting in either more borrowings with interest liability or cutting of developmental/welfare activities to that extent.

Bringing in the concept of non-performing assets to public finance would attract due attention and facilitate executive accountability.

4.8 Sale and utilisation of assets – within the executive power of government

The Constitution vested all public properties, assets, lands, minerals, other things of value underlying the ocean within the territorial waters and in the continental shelf with the Union/States (Articles 294 to 297). The Constitution, also, leaves the further acquisition, holding and disposal of the property and making of contracts for any purpose to the Executive power of the Union and States (Article 298). Thus, managing and sale of these assets, fixation of sale value, rent, etc., are within the executive power of the government.

4.8.1 Increasing private participation

The concepts liberalisation and privatisation redefine the role of government. With the advent of these concepts, many activities hitherto done by the government or through government undertakings are being opened to private parties with new ideas/arrangements like Build, Operate and Transfer (BOT), Build, Own, Operate and Transfer (BOOT), Public Private Participation, Profit sharing contracts, etc. Under these arrangements, the public assets either become commodities (like minerals, petroleum) or get used by the private parties (like land for lease rent).

The case of mining operation may be a typical example to indicate the trend of private participation. As per the Industrial Policy Resolution, 1956, major minerals such as coal, lignite, mineral oil, iron ore, copper, atomic minerals, etc., were reserved exclusively for the public sector. The Comprehensive National Mineral Policy (NMP) announced in March 1993, encouraging private investment including Foreign Direct Investment (FDI) in exploration and mining, mining operations in major minerals opened-up to these areas to the private sector. The position has been further eased in the following period.

4.8.2 Power of executive government to vary rates of revenue charges

The executive government is empowered to vary (increase/reduce) the rates of certain non-tax revenues without requiring any further approval therefor from the Parliament/State Legislature.

For instance, as per Sections 9 (3) and 9A (2) of Mines and Minerals (Development and Regulation) Act 1957, as amended up to April 2012, the Central Government may, by notification in the Official Gazette, can enhance or reduce the rate of royalty payable in respect of any mineral and dead rent payable by the lessee.

The above position coupled with more private participation would indicate the seriousness of the accountability issue and proneness of the system.

4.8.3 Some policy decisions without knowledge of the Parliament

Sometimes, policy decisions not involving legislative aspects are not specifically discussed in the Parliament. For instance, the New Telecom Policy (NTP), 1999 was not discussed in the Parliament, as may be noted from the following passage in the Report of the Joint Parliamentary Committee to examine the matters relating to allocation and pricing of Telecom Licenses and Spectrum:

"Regarding the desirability of a discussion on the new telecom package when the new parliament was to be constituted at a later date, it was clarified that the New Telecom Policy (NTP), 1999, which was approved by the Cabinet on 26th March 1999 was neither specifically discussed in Parliament nor was this necessary to do so particularly so no legislative aspect was involved. A copy of the policy was, however, placed in the Parliament Library/Parliament Secretariat." (Report of JPC, 2013 para 3.10

All the above indicates more executive actions with significant ramifications on the public finance without knowledge of the Parliament/Legislature. In the absence of any system for transparency and accountability, no outsiders would come to know whether all the revenue dues have been realised or not.

4.9 To make tax collection machinery robust and accountable

The details of non-levy and quantum of uncollected dues would provide the basis for evaluating the efficiency/adequacy of the revenue collection system.

The need for robust tax collecting machinery was observed by the Supreme Court of India on the writ petition relating to black money as follows (Ram Jethmalani & Ors vs Union Of India & Ors 2011):

"… Secondly, large quanta of monies stashed abroad, would also indicate a substantial weakness in the capacity of the State in collection of taxes on incomes generated by individuals and other legal entities within the country. The generation of such revenues is essential for the State to undertake the various public goods and services that it is constitutionally mandated, and normatively expected by its citizenry, to provide. A substantial degree of incapacity, in the above respect, would be an indicia of the degree of failure of the State; and beyond a particular point, the State may spin into a vicious cycle of declining moral authority, thereby causing the incidence of unlawful activities in which wealth is sought to be generated, as well as instances of tax evasion, to increase in volume and in intensity." (ibid, paragraph 8)

"…….The strength of tax collection machinery can, and ought to be, expected to have a direct bearing on the revenues collected by the State. If the machinery is weak, understaffed, ideologically motivated to look the other way, or the agents motivated by not so salubrious motives, the amount of revenue collected by the State would decline, stagnate, or may not generate the revenue for the State that is consonant with its responsibilities. …… (ibid, paragraph 14)

A system for complete disclosure of unrealised revenue and its reporting to the Parliament would bring a continuous machinery for monitoring tax-collections.

V Feasibility of preparation of proposed Receipts Accounts

5.1 Types of government receipts and flexibility of existing accounting system

The receipts of the governments and the major heads of accounts therefore are as follows:

Tax Revenues	0020 to 0045
Non-tax Revenue	0046 to 1475
Grants-in-aid/contributions	1601 to 1606
Capital Receipts	4000
Borrowings	6001 to 6005
Loans and advances given by government	6075 to 7615

As detailed in paragraph 2.2 above, the 6-tier government accounting system consists of various tiers below with a coding pattern. Interestingly, it provides for accounting of refund of tax revenue by opening of a separate sub-head under appropriate minor head, so that the net collection of each tax could be ascertained. For refund of Non-tax revenue, the classification provides for specific minor head viz., "Deduct – Refunds" (code 900).

Similarly, there are provisions for accounting of recoveries of overpayments/refund of expenditure. If it is made in the same year, it would be treated as a reduction of expenditure. When they relate to previous years, they are to be accounted under a distinct minor head '911 Deduct – Recoveries of over payments' below the relevant major/sub major head of expenditure so that current year's expenditure could be ascertained.

From the above, it may be clear that there are lots of scope for introduction of additional codes to meet requirements like dues, demand raised, etc., within the existing accounting system with suitable modifications. Alternatively, proposed Receipts Accounts may be prepared outside the government accounting system also, as detailed in the subsequent paragraph, 5.2.

5.2 Availability of data/inputs for the proposed Accounts

Of various government receipts, the actual revenues of the governments are taxes and non-tax receipts and capital receipts (other than borrowings and loans and advances). Government has no control over the grants-in-aid/contributions received. Thus, the system for monitoring of realisation of revenues requires only tax and non-tax revenues and miscellaneous capital receipts.

In the existing system two details viz., Budget Estimates for receipts and Actual receipts are available. The comparison of these two would disclose the level of accuracy of estimates prepared or level of performance against the estimates.

The other inputs required for arriving at the unrealised revenue are

- Amount to be levied
- Amount levied/demand raised
- Amount actually collected

Of the above, arriving at the amounts to be levied in respect of Tax revenue would only be a big challenge, while that of for non-tax revenue (mostly in the nature interest, fees for services, Royalty, leasing charges, rent, receipts on account of profit-sharing arrangement) could be easily ascertained loan/lease agreements, etc. The details of amount levied/demanded and collected would always be available with the departments concerned.

For the amounts to be levied in respect of tax revenues, a non-financial account containing details of number of assesses registered with the department, the number of assesses not filed the return, number of returns not assessed/demand raised, etc., may be maintained. These positions of returns not filed and non-assessed would provide a base to pursue the cases, besides ensuring the continuity/control over the cases of unpaid taxes/unfiled returns.

5.3 Model of Accounts proposed

The proposed accounts shall contain all information like total revenue due (physical data like total assessed for tax revenue), demand raised, amount collected and balance remains to be levied/collected with reasons therefor. If feasible, the details of individuals/entities with significant dues can also be included.

In view of its uniqueness, the model Appropriation Accounts could only be adopted with appropriate modifications. Therefore, the proposed Accounts may be made into two parts, viz., (i) Summary of revenue/receipts giving overall position and (ii) Detailed part with more information. While, the Summary part would depict the actual collection during the year compared to the total due including arrears and Budget Estimates, the Detailed part would give Head wise details of receipts realised and not realised with reasons for non-realisation. The formats for the same are given below:

A. Summary of receipts

1. Tax Revenue

Major Head	Description	Opening Balance	Demand Made during the year	Out of OB		Out of current demand		Closing Balance
				Collected	Settled	Collected	settled	
0020	Corporation Tax							
0021								

2. Non-tax Revenue

Major Head	Description	Opening Balance	Demand Made during the year	Out of OB		Out of current demand		Closing Balance
				Collected	Settled	Collected	settled	
	Interest							
	Royalty							

3. Capital Receipts (non-debt)

Major Head	Description	Opening Balance	Demand Made during the year	Out of OB		Out of current demand		Closing Balance
				Collected	Settled	Collected	settled	
	Dividend							

B 1 Detailed Receipts Accounts (Tax Assessments)
Two separate tables (a) and (b) – for each Major Head

a) Details of returns filed (Major Head wise)

OB of Returns not filed	No. of Assessees for the year	No. of Assessees filed Returns during the year		Total pendency in filing of returns at the end of year
		for previous years	for current year	

i. Reasons for increasing trend of pendency (if so) in filing the returns.
ii. Details of major actions taken to get the returns filed

b) Details of assessments/demands made (Major head-wise)

No of assessments pending at beginning of the year	No. of Assessees filed Returns during the year	No. of cases assessed during the year		No of assessments pending at the end of the year
		Of previous years	Of current year	

a. Reasons for non-assessment of cases
b. Details of major actions taken for completion of assessment

B 2 Detailed Receipts Accounts (Tax revenue)

c) Details of amount realised and not realised (Minor head wise or Region-wise)
Major Head:

Minor Head/ Region	Description	Opening Balance	Demand Made during the year	Out of OB		Out of current demand		Closing Balance
				Collected	Settled	Collected	settled	

i. Reasons for the pendency of items beyond a limit (may be prescribed by PAC)
ii. Reasons for settlement of items beyond a limit (may be prescribed by PAC

Amount under dispute						Amount not under dispute						Grand Total
over 10 years	over 5 years	over 2 years	over 1 year	current year	Total	over 10 years	over 5 years	over 2 years	over 1 year	current year	Total	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)

d) Details of unrealised receipts (Minor head wise or Region-wise)

(i) For the amount under dispute -Significant reasons for pendency/dispute
(ii) For the amount not under dispute - Significant reasons for the pendency
Details of significant items (i.e limit as may be prescribed by PAC) under both the categories with action taken/present stage of the case/collection

The formats for Detailed Receipts accounts for non-tax revenues and Capital Receipts (Non-debt) may be (c) and (d), department-wise.

5.4 Preparation and certification of Receipts Accounts

In accordance with the existing arrangement, compilation and preparation of the proposed Receipts Accounts may also be entrusted to the same organisation/authority which is now preparing the Finance and Appropriation Accounts. Alternatively, accounts may be prepared by the major tax collecting Department concerned and the Finance Ministry for all minor taxes non-tax revenues.

The proposed Accounts should, however, be required to be certified by the Comptroller and Auditor General of India before presenting them to the President/Governor.

VI Conclusion

The accountability and transparency, and efficiency and effectiveness expected of in spending should equally apply to revenue collection also, as the effectiveness of financial management depends on both revenue realisation and quality of spending.

The extant system of parliamentary control is not complete in respect of revenue collections. Consequently, crores of public revenue remain uncollected without the knowledge of Parliament and people of the country depriving the benefit of public scrutiny of revenue collecting machinery of the government.

In the scenario of emerging trends with more and more private participation and allowing them to utilise public assets and properties, it is imperative to have a robust mechanism to ensure closer monitoring of revenue collection by the Parliament/Legislature, besides ensuring adequate transparency for public scrutiny.

Road map: Either suitable explicit statutory provision is to be made for preparation of a Receipt Accounts and its submission to the Parliament/State Legislature or CAG shall exercise his authority under Article 150 for prescribing appropriate form of accounts for a Receipts Accounts.

References

Budget documents for 2021-22 presented to the Parliament (https://www.indiabudget.gov.in/)

Budgetary process – information Bulletin, Lok Sabha Secretariat, New Delhi, July 2014(https://eparlib.nic.in/handle/123456789/247?view_type=search)

The Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971 (https://cag.gov.in/en/page-duties-power-and-conditions-of-services-act)

Constituent Assembly debates (proceedings) (http://164.100.47.194/Loksabha/Debates/cadebadvsearch.aspx)

Constitution of India, Various Articles

Finance and Appropriation Accounts of Union government (www.cga.nic.in) and State governments available at www.cag.gov.in

List of Major and Minor Heads of Accounts (LMMHA) of Union and States issued by the Controller General of Accounts (https://cga.nic.in/Book/Published/list.aspx)

Mines and Minerals (Development and Regulation) Act 1957, as amended up to April 2012

National Mineral policy, 1993 (https://mines.gov.in/writereaddata/UploadFile/Policy_Legislation_more.pdf)

Parliamentary question (Unstarred question No.3945) answered on 26th August 2011 in the Parliament by the Minister of State in the Ministry of Finance (http://164.100.47.194/Loksabha/Questions/QResult15.aspx?qref=111118&lsno=15)

The Fiscal Responsibility and Budget Management Act, 2003 and Rules 2004

Receipt Budget of Union 2021-22 (https://www.indiabudget.gov.in/budget2021-22/doc/rec/allrec.pdf)

Revenue Audit Manual on Direct Taxes, Comptroller and Auditor General of India, 2015 (https://cag.gov.in/uploads/manuals/manual-manuals-05de7511d785829-96279608.pdf)

Comptroller and Auditor General of India. 2014. "Service Tax Administration." https://cag.gov.in/uploads/download_audit_report/2014/Union_Compliance_In_Direct_Tax_Service_Tax_Revenue_Dept_6_2014_Chapter_1.pdf

Comptroller and Auditor General of India. 2021. *Report on the Accounts of the Union Government - Financial Audit.* Report No 7, New Delhi: Union Government.

Association of Unified Tele Services providers & Others vs Union of India & Others, WP(C) NO. 3673/2010, Delhi High Court, 6 January 2014, https://indiankanoon.org/doc/49362073/.

Association of Unified Tele Services providers & Others vs Union of India, CIVIL APPEAL NO. 4591 OF 2014, Supreme Court of India, 17 April 2014 . https://indiankanoon.org/doc/112886265/.

Ram Jethmalani & Ors vs Union Of India & Ors. 2011. WRIT PETITION (CIVIL) NO. 176 OF 2009 (Supreme Court of India, https://indiankanoon.org/doc/1232445/ July 4).

Report of Joint Parliamentary Committee (JPC) to examine matters relating to allocation and pricing of Telecom Licences and Spectrum (Fifteenth Lok Sabha), Lok Sabha Secretariat, New Delhi, October 2013

https://eparlib.nic.in/handle/123456789/783369?view_type=browse

Reports of Comptroller and Auditor General of India available at www.cag.gov.in

Notes

[1] The system of accounting under which the receipts and expenditure are recognized as and when collected/paid; moneys due to or due by the entity is not shown in the accounts

[2] Section 11: The CAG shall from the accounts compiled by him or by the Government or any other person responsible in that behalf prepare in each year accounts (including, in the case of accounts compiled by him, appropriation accounts) showing under the respective heads the annual receipts and disbursements for the purpose of the Union, of each State and of each Union territory having a Legislative Assembly, and shall submit those accounts to the President or the Governor of a State or Administrator of the Union territory having a Legislative Assembly, as the case may be on or before such dates as he may, with the concurrence of the Government concerned, determine (with further provisos for relieving CAG from preparation and submission of the accounts).

[3] Fiscal deficit is the excess of total expenditure including repayment of debt charges over the total receipts including receipts from the sale of assets but excluding the borrowing during a financial year. This indicates the shortage of receipts to meet the expenditure and the shortage is to be managed by borrowing.

[4] Finding the traditional methods of managing fiscal deficit by printing of more money or using the foreign exchange reserve ineffective, the main source to fill the deficit is, now, generally borrowing

INSTRUCTIONS TO AUTHORS

IPPR is a peer-reviewed, bi-monthly, online, and an open-access journal to facilitate scholarly communication of research on public policies, especially in the Indian context. IPPR invites original unpublished theoretical and empirical papers with a bearing on policy. In particular, the papers are invited in the fields of economics, political science, science and technology, international relations and defence strategy and security.

Submitting Your Paper

Please submit your papers here: http://www.ippr.in/index.php/ippr/about/submissions

Peer Review

All manuscript submissions are subject to editorial screening and anonymous peer review. All editorial decisions in this respect will be final. Average paper turnaround time will be 120 days.

Preparing Your Paper

Contributors should submit original unpublished articles for publication. Authors are advised to not submit work that they have submitted elsewhere.

Please include a word count for your paper.

- Research paper for IPPR should be more than 5000 words and less than 8000 words.
- Commentary for IPPR should not exceed 2500 words.
- Book review for IPPR should be within 800-1000 words.

Writing Guidelines

- Research papers should carry a 200-word abstract and a maximum of six key words.
- If your paper is in the domain of economics, please include the relevant JEL codes, based on the keywords.
- Please use British oxford spellings throughout the manuscript.
- Please use single quotation marks. If the quotation is long, it should be indented without using the quotation marks.
- Please write dates in a month-date-year sequence (Ex: December 5, 2019)
- While referring to numbers till Nine, please write in text and then in numerals.
- At first mention, acronyms should carry their full forms and abbreviations in bracket. Thereafter, the abbreviated version should be used.
- Please include a short bio of each author towards the end of the manuscript.
- If research is funded by external agencies, all funding details for the research should be provided.

Referencing and endnotes

- All manuscripts will be thoroughly checked for plagiarism. Authors are responsible for the accuracy of their referencing.
- Use in-text parenthetical citation while referring to the works of others, with author name(s), date, and page numbers, where applicable. The full details of the reference can be provided in the bibliography at the end.
- Please use Chicago style of referencing for the bibliography. For examples of referencing styles, please refer to: https://www.chicagomanualofstyle.org/tools_citationguide/citation-guide-2.html
- If two successive citations/notes refer to the same source, use ibid.
- For any online reference, please provide the date accessed along with other information.
- Endnotes must be separate from the citations and must not be used to provide a reference. It can be used to explain or elaborate on an idea in the text.

Document

- Please submit both a PDF and an editable word document of your paper. This will help us format the document.
- If the article uses any supplementary material, such as a table, graph, maps, etc, an editable document of the data source (Word, Excel, etc.) should be provided.
- Each table, graph, etc. should be numbered, have a legend and a heading.

Copyright

- IPPR will post all published articles on its websites and summaries or excerpts maybe published on other digital and print properties.
- The copyright of all articles published in IPPR will belong to the author(s) or their institution depending on the author's terms of employment.